WAWANESA INSURANCE ANNUAL REPORT 2007

SUBSIDIARY COMPANIES

THE WAWANESA LIFE INSURANCE COMPANY

200–191 Broadway
Winnipeg, Manitoba R3C 3P1

100% Owned
Book value of shares $54,365,000

WAWANESA GENERAL INSURANCE COMPANY

9050 Friars Road
San Diego, California 92108

100% Owned
Book value of shares $113,598,000

President's Report

It was indeed an honour and privilege to be appointed President & Chief Executive Officer of Wawanesa in May of 2007. I will work to ensure that we continue to progress as a strong and growing company in the years ahead. It is with great pride that I present my first report to Wawanesa policyholders regarding the condition of our company and the financial results for 2007.

The past year was truly an eventful one with many challenges and developments. Perhaps the most significant development was the decision to terminate the major system replacement project known as OWASYS. As well, there were a few personnel changes within senior management and the Board of Directors. More about these items later in the report.

Before moving into a review of the year's results, I would like to make a few observations and comment on a few initiatives that began during the year which I think are important in preparing our company for the future. Wawanesa Mutual has grown substantially in recent years such that we now report written premium income in excess of $1.8 billion while servicing over 1.7 million policyholders. The various environments in which we operate have become much more complex. There continues to be increased government regulation in the design and pricing of our products, increased regulatory and rating agency attention, increased corporate governance expectations and increased privacy and security requirements. Competition from product/price and service standpoints is increasing such that our products and services have become more complex and change more frequently. The nature of the risks we insure and the exposures represented by those risks have also become more complex. Our policyholders and brokers rightfully expect improving service levels. This increased size and environmental complexity drives the need for us to develop a more structured organization, better prepared to appropriately address future challenges and ensure our company remains a respected insurance provider in the years ahead. We must develop internal policies that address the requirements of various regulators and stakeholders and must also be able to demonstrate the effectiveness of those policies. We must ensure we have capable staff members who are well-trained to provide required service levels. And clearly we must implement improved information systems to support our business in an effective and efficient manner. These are the challenges of the next few years.

In this regard, during 2007 we entered the early stages of a number of significant initiatives. We started the development of a formal business planning and financial reporting process which will be developed further in the next couple of years. This will allow for better planning and monitoring of our business operations. We are reviewing our approach to staff development and succession planning. We have reorganized our Information Services department and implemented changes to our planning and monitoring of all levels of computer systems work, from routine maintenance to major projects. The intention is to ensure the department delivers service to business operations in an effective and timely manner. These initiatives and others are not designed to change who we are but rather to ensure the organization is well prepared to stay relevant to our stakeholders in the years ahead. They are more in the nature of transforming internal processes than specific projects. We are in great financial shape, are certainly well respected and want to ensure that does not change.

FINANCIAL RESULTS

New accounting principles related to valuation of financial instruments were recently introduced and were adopted by Wawanesa for 2007. The changes primarily impacted the valuation of investments on the balance sheet of the company and reporting of certain types of investment income. For 2007, we are reporting an underwriting loss of $60 million, in sharp contrast to an underwriting profit of $58 million in 2006. Our change in fortunes was largely the result of weather-related claim events but also from generally deteriorating

results in a couple of regions in the final quarter of the year. We experienced a record year of claim catastrophes with 15 events totaling losses of $108 million. After reinsurance, our exposure was $78 million. However, realized investment income was strong at $235 million and after incorporating the income of Wawanesa Life, our net income for the year was $116 million. The size of the company continued to grow in 2007. Premium income grew by 1.9% to just over $1.8 billion. Invested assets increased and now have a market value of $3.8 billion. As a result of income earned in the year, our surplus increased to $1.85 billion. The new accounting principles introduced a new financial statement item, Total Equity, which is now included on the balance sheet. This represents our accumulated surplus plus certain other financial items such as unrealized gains on investments and the financial effect of conducting a portion of our operation in US$. Total Equity is reported at $1.95 billion.

MARKET OBSERVATIONS

We are experiencing generally soft markets in all regions. This means that it is a very competitive environment which makes it more difficult to grow. However, we did grow our policy count modestly (2.3%) during the year with most areas showing some growth. Only Ontario and Quebec reported slight reductions in policy counts.

The entire industry (including Wawanesa) is currently facing a significant challenge in the Alberta automobile market. The Minor Injury Regulation (MIR) was struck down as being inconsistent with the Constitution Act, 1982 and was found to offend the Canadian Charter of Rights and Freedoms. The MIR was established in 2004 as part of a comprehensive overhaul of the automobile insurance system designed to ensure affordability of insurance in the province. The government has indicated its intention to appeal the decision but the uncertainty of the legal status of the regulation results in an unsettled situation for insurers, policyholders and claimants.

REGIONAL RESULTS & CONDITIONS

In the Maritimes we had excellent overall results in 2007 including continued strong growth and great financial results. We responded to government challenges in New Brunswick by being a major contributor to the new industry-developed territory pricing structure and by introducing our own eight territory structure. There was strong cooperation between branch and executive office staff in developing the new structure.

In Quebec we have experienced declining business for the last few years. In response, we launched a multi-faceted initiative in early 2007 to address the situation including rate changes, sales force incentives and a new web site with excellent quoting capabilities which was introduced in February of 2008. New business is increasing and retention rates are improving while profitability is acceptable. We look forward to growth in Quebec in 2008 and beyond.

Ontario has been a very competitive market for the last few years and 2007 was no different. We did not grow our business in 2007 but our staff worked hard to keep our service levels and business retention high. As Ontario Branch had been selected for initial implementation of the OWASYS project, there was much focus during the year on preparing for that event.

Winnipeg Branch experienced reasonable growth in 2007 especially considering our already strong market share. Financial results were affected by weather-related claims catastrophes totaling $6 million.

Prairie Branch also generated growth in the year and achieved the $100 million written premium level during 2007. The branch was heavily affected by weather-related claims to the extent of $35 million, particularly a wind and hail storm that struck parts of both Saskatchewan and Manitoba in August and inflicted serious damage in Dauphin, Manitoba. Losses from that storm totaled $21 million. Even without the claim catastrophes, financial results were a struggle in 2007. Premium rate increases were taken in property lines.

2 THE PAST YEAR WAS TRULY AN EVENTFUL ONE WITH MANY CHALLENGES AND DEVELOPMENT

Good growth was experienced in both Alberta branches in 2007. Both faced a significant number of weather-related catastrophes resulting in total claim catastrophe costs of $27 million in each branch. Also, due to the strong Alberta economy, both faced claims service provider availability problems and staffing challenges. However, that's where the similarities end. Southern Alberta Branch had an amazing year. Even after dealing with the claim catastrophes, the branch still reported a near break-even financial result. By contrast, Northern Alberta's financial results for 2007 were not good even without the catastrophe totals. An exceptional number of fire losses early in the year, combined with generally deteriorating results as the year progressed, contributed to a disappointing financial result.

In British Columbia, we experienced good growth and quite acceptable financial results. The year started with heavy rain storms in January but results gradually improved throughout the remainder of the year. Special thanks are extended to branch staff and management who ensured the branch operated well during the absence of our Regional Vice President for a number of months.

Our United States Operations reported an excellent year of growth, 4.8% by policy count. However, a rate reduction in December of 2006 precluded premium growth. California is currently a very competitive automobile market. The US operation was exposed to the wildfires that occurred in Southern California in October. Many policyholders and some of our staff members were affected. We handled hundreds of claims including a number of total losses totaling $13 million. Almost all of these claims have now been settled and not one complaint has been received. That is a testament to the special efforts made by our claims staff during those difficult times. In addition to these claims, financial results were also impacted by generally deteriorating results in the 4th quarter resulting in a significant underwriting loss in the US Operations and a small overall loss in Wawanesa General, our US subsidiary company.

The record level of catastrophic claim activity put strain on our claims operations in many parts of the company. It is satisfying to note that all situations were handled well given the specific circumstances. In many of these situations, special arrangements were implemented to ensure that our customers were serviced quickly and effectively. Thank you to all claims staff for their commitment to our customers during these challenging events. We often say that our claims service is our best advertising and I believe we had some great advertising this year.

INFORMATION SERVICES

Development of the next generation of computer systems to replace our current insurance administration and claims processing system has been both a priority and a challenge. Currently, we are focusing our information systems efforts in the following directions:

- During 2008, we will work to develop an appropriate systems replacement strategy that is linked to our overall business strategy. It is envisioned that such a strategy will be component-based rather than attempting to replace policy, claims and billing systems all at one time. Our experience now shows that there is no one software system that can replace all of the existing systems.
- We will emphasize maintaining and upgrading our existing systems to ensure they continue to function effectively while we develop a replacement strategy. These systems have been in existence for some time, and while they lack some desired functionality, are quite stable.
- We will continue to work on our Broker Portal initiative which will provide for transaction connectivity with brokers to ensure efficiency in our business relationship with our broker partners.
- Finally, we are further developing our overall capabilities to ensure we can effectively deliver system enhancements as required by the growth in our business.

In 2004, the OWASYS Project was initiated to provide the next generation of core processing systems. The intent of the OWASYS Project was to develop a system that would replace the Company's policy, claims and billing systems all at one time. We had purchased a system from a software vendor and engaged outside consultants to guide us with the development and customization of the system. The process involved considerable time and effort, however, many timing delays were encountered and it became evident that original functionality requirements and time lines would not be met.

In February, 2007, management recommended a thorough review of the project be undertaken. The services of an acknowledged systems expert were engaged to perform the review and present findings to the Company. The findings were reviewed by the Board with the systems expert in September, 2007 and the Board asked management to study the report and give an account to the Board with its recommendations. In October, 2007, management recommended the project be terminated and the Board concurred.

This decision was not made lightly. The Company expended an aggregate of $80 million from 2004–2007 on the OWASYS project. It was, however, concluded that in spite of these expenditures, the continuation of the project was not the appropriate approach to upgrading our information system and technology environment. Of the expenditures, approximately $10 million represents future value to the Company and will benefit our ongoing Information Services programs.

OWASYS was an investment in innovation that was not successful. However, the lessons learned are invaluable as we continue to develop and improve our information systems and service.

WAWANESA LIFE

The past year was a positive one for Wawanesa Life. Growth in business and good profitability were experienced. New accounting principles related to valuation of financial instruments were adopted for 2007. Total assets under administration, including segregated funds, have increased by $61.3 million to reach a total of $637 million. This is the result of both overall growth and the accounting changes requiring investments to be recorded at their current fair value. This increase in asset values is generally offset by a corresponding increase in policy liabilities and segregated fund contract liabilities.

Overall premium income grew to $85.9 million, an increase of $5.1 million over 2006.

Investment income is down $4.0 million compared to 2006 due to the changes in financial reporting noted above. Because of the close relationship between invested assets and policy liabilities, changes in the fair value of assets produced a similar offsetting change in actuarial reserves. Other factors affecting the change in reserves in 2007 include increased reserve obligations due to new business sales and the release of prior reserves due to revised assumptions and better asset/liability matching. Other individual benefit and expense categories are tracking at consistent levels given the growth in the business while group benefits payments have shown considerable improvement over 2006.

The net result is income before tax of $9.5 million and $7.3 million after tax. The new financial reporting requirements have introduced a new income category called Other Comprehensive Income/Loss which captures the unrealized changes in the fair value of assets used to support the Company's capital and surplus. Adding reported net income and other comprehensive loss for the year results in total comprehensive income of $4.9 million after tax compared to $5.8 million after tax in 2006.

Sales records continue to be set and broken in the Individual Operation. This year's achievement of $5 million in gross annual sales establishes another best ever performance and is the 4th year in a row that new business targets have been met or exceeded. However, this new level of success has introduced some operational challenges in the policy issue departments. As such, there are plans to review many internal processes with the intention of

GROWTH IN BUSINESS AND GOOD PROFITABILITY WERE EXPERIENCED

maximizing operational efficiency while lessening the workload being experienced in these departments.

Sales success has also been witnessed in the Group Operation this year. In the third quarter, new business premium increased by a very healthy $900,000 and by another $1 million in the fourth quarter to produce a year end total of $2.8 million. As well, the Group Operation experienced improvement in its claims experience across all lines of business, with the most notable improvement being in long-term disability. This has returned the Group Operation to a comfortable profit position, a position that has been achieved for six out of the last seven years.

The implementation of the Eclipse system in the Group Operation has passed its final hurdle with the launch of the member site in mid-December. This site allows individual plan members to track the status of their claims, view their claims history and update basic enrolment information in addition to allowing plan administrators to manage their member data electronically. This online administration capability is the end result of a four year process involving the system selection, development, testing and implementation phases, and meets our goal of bringing online technology to our group policyholders and plan members. Online administration brings transparency to our clients and efficiencies to Wawanesa Life. This success does not mean that development will stop. Rather, the Eclipse team will continue to look for ways to meet and exceed our broker/client expectations.

ACKNOWLEDGEMENTS

It's old news now, but it is appropriate to observe that Gregg Hanson, our President & CEO for 15 years, retired from the position in May, 2007. Gregg's dedication to the Company spans 28 years and will continue in the future as he continues to serve as a member of the Board of Directors. We again thank Gregg for his significant contribution to Wawanesa. Gregg's contribution to the company and the industry was observed at a number of functions in the spring of 2007.

John Bjornson, Vice President, Property Underwriting and Marketing, retired this year after almost 40 years with the Company. John served the Company in a variety of roles including those of a junior member of the newly formed computer operation in 1968, Regional Vice President of Prairie Branch from 1987–1992 and his final position which he held from 1999. We thank John for his contribution over many years. As a result of John's retirement, Jeff Goy added the property insurance portfolio to his existing auto responsibilities and was appointed Vice President, Insurance Products. There is no doubt that Jeff will make a significant contribution in his expanded role.

Gary Timlick, B.Comm. (Hons.), C.A., joined us as Vice President & Chief Financial Officer in February, 2008. Gary is a chartered accountant with excellent experience who previously served as Chief Financial Officer with two significant Manitoba organizations. Gary will be responsible for all financial operations of our organization including financial reporting, investment oversight, treasury and risk management.

Two members of our Board of Directors decided to resign in late 2007 after many years as effective and contributing Board members. Brian Ransom served the Board for 19 years while Duncan Jessiman served for 14 years. We thank both of them for their dedication to Wawanesa over many years of service.

I would like to thank the great staff of Wawanesa for their continued commitment and dedication. The support you have provided me with in my new position is truly gratifying. I also want to offer a thank you to our brokers who continue to support us. We are working hard to justify your commitment to Wawanesa.

Ken McCrea, CA, FLMI
President and Chief Executive Officer

Founded in 1896
Incorporated May 1, 1929

Head Office
Wawanesa, Manitoba

Executive Office
900–191 Broadway
Winnipeg, Manitoba

OFFICERS AND CORPORATE MANAGEMENT

K. E. McCrea, CA, FLMI
President and Chief Executive Officer

G. N. Bass, Q.C.
Vice President, General Counsel and Secretary

B. A. MacKinnon, FCAS, FCIA, MAAA
Vice President and Chief Actuary

G. J. Timlick, CA
Vice President and Chief Financial Officer

P. R. Goodman, CA
Vice President and Comptroller

S. J. Goy, ACAS, CIP
Vice President, Insurance Products

R. G. LaPage, FCIP, CRM
Vice President, Claims

C. R. Loeppky, BScCS
Vice President, Information Services

C. B. Luby, FCIP, CRM
Vice President, Branch Operations

T. L. Nelson, FLMI/M, CHRP, CIP
Vice President, Human Resources

P. R. Mulaire, CMA, FCIP, CIA
Manager, Internal Audit

To the Directors of The Wawanesa Mutual Insurance Company

We have audited the consolidated balance sheet of **The Wawanesa Mutual Insurance Company** as at December 31, 2007 and the consolidated statements of operations, equity, comprehensive income and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

Note 4 describes the policy with respect to the non-consolidation of a 100% owned subsidiary, The Wawanesa Life Insurance Company, whereby the investment is recorded on the equity basis. In this respect, the consolidated financial statements are not in accordance with Canadian generally accepted accounting principles. Note 6 includes information on significant balance sheet and income statement items of the subsidiary. Had the financial statements of the subsidiary been consolidated, virtually every account in, and the information provided by way of notes to, the accompanying consolidated financial statements would have been affected by the underlying information of the subsidiary.

In our opinion, except for the effect of not consolidating The Wawanesa Life Insurance Company, as described in the preceding paragraph, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants
February 27, 2008, Winnipeg, Manitoba

PRICEWATERHOUSECOOPERS

THE WAWANESA MUTUAL INSURANCE COMPANY

To the Directors of The Wawanesa Mutual Insurance Company

I have valued the policy liabilities of the Company for its consolidated balance sheet as at December 31, 2007 and their change in the consolidated statement of operations for the year then ended in accordance with accepted actuarial practice including selection of appropriate assumptions and methods.

In my opinion the amount of policy liabilities makes appropriate provision for all policyholder obligations, and the consolidated financial statements fairly present the result of the valuation.

Brett A. MacKinnon

Brett A. MacKinnon, FCAS, FCIA, MAAA
February 27, 2008, Winnipeg, Manitoba

BRANCH OFFICES

Maritime
1010 St. George Boulevard
Moncton, New Brunswick
S. M. Gates, CHRP
Vice President, Maritime Region

Québec
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C. Auclair, PAA
Vice President, Québec Region

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T. R. Greer
Vice President, Ontario Region

Winnipeg
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Winnipeg, Manitoba
E. Rossong, FCIP
Vice President, Winnipeg Region

Prairie
Wawanesa, Manitoba
W. G. McGregor, FCIP
Vice President, Prairie Region

Northern Alberta
100, 8657–51st Avenue
Edmonton, Alberta
N. D. Miller, FCIP
Vice President, Northern Alberta Region

Southern Alberta
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J. A. Breau
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K. L. Coates, FCIP, FRM
Vice President, British Columbia Region

United States
9050 Friars Road
San Diego, California
D. J. Goss
Vice President, United States Operations

CONSOLIDATED BALANCE SHEET

	As at December 31	
	2007	2006 (note 3)
	('000s)	
Assets		
Investments (note 5)	**$ 3,820,995**	$ 3,410,774
Accrued investment income	**22,794**	23,655
Receivables	**455,001**	415,805
Income taxes receivable	**80,675**	–
Investment in subsidiary (note 6)	**54,365**	43,939
Real estate – at cost, less accumulated depreciation of $28,118 (2006 – $26,411)	**42,939**	46,770
Furniture and equipment – at cost, less accumulated depreciation	**12,654**	12,851
Due from Facility Association	**14,930**	21,651
Deferred acquisition expenses	**142,642**	135,455
Future income taxes (note 9)	**16,219**	142,186
Total assets	**$ 4,663,214**	$ 4,253,086
Liabilities and Equity		
Bank indebtedness	**$ 6,537**	$ 26,821
Unpaid claims (note 7)	**1,678,460**	1,520,948
Income taxes payable	**–**	13,133
Other liabilities	**122,601**	111,826
Unearned premiums	**889,472**	878,490
Mortgage payable (note 10)	**12,998**	13,188
Total liabilities	**2,710,068**	2,564,406
Total equity	**1,953,146**	1,688,680
Total liabilities and equity	**$ 4,663,214**	$ 4,253,086

THE WAWANESA MUTUAL INSURANCE COMPANY

The accompanying notes constitute an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENT OF OPERATIONS

	For the year ended December 31			
	2007		2006 (note 3)	
	('000s)			
Gross premiums written		**$ 1,808,837**		$ 1,775,698
Premiums ceded (net)		**(35,775)**		(36,166)
Net premiums written		**1,773,062**		1,739,532
Increase in unearned premiums		**(35,412)**		(48,425)
Net premiums earned		**1,737,650**		1,691,107
Instalment service charges earned		**24,025**		22,963
		1,761,675		1,714,070
Deduct: Claims incurred	**$ 1,355,535**		$ 1,215,334	
Expenses incurred	**466,076**	**1,821,611**	440,664	1,655,998
Underwriting gain (loss)		**(59,936)**		58,072
Net investment income				
Realized gains on sale of investments		–		59,963
Realized gains on sale of available-for-sale assets		**91,167**		–
Other net investment income (note 5)		**144,157**		139,766
		235,324		199,729
Income before income taxes		**175,388**		257,801
Income taxes (note 9)				
Current	**58,143**		126,172	
Future	**6,031**	**64,174**	(33,041)	93,131
Income before the following		**111,214**		164,670
Income from subsidiary		**4,562**		2,430
Net income for the year		**$ 115,776**		$ 167,100

The accompanying notes constitute an integral part of the consolidated financial statements.

The Wawanesa Mutual Insurance Company

CONSOLIDATED STATEMENT OF EQUITY

	For the year ended December 31	
	2007	2006 (note 3)
	('000s)	
Retained earnings		
Balance – beginning of year, as previously reported	**$ 1,688,680**	$ 1,522,004
Adjustment for change in accounting policy (note 3)	**49,265**	37,306
Balance after change in accounting policy	**1,737,945**	1,559,310
Net income	**115,776**	167,100
Balance – end of year	**1,853,721**	1,726,410
Accumulated other comprehensive income (loss) – net of taxes		
Balance – beginning of year, as a result of change in accounting policy (note 3)	**252,875**	(37,306)
Total other comprehensive loss	**(153,450)**	(424)
Balance – end of year	**99,425**	(37,730)
Total equity	**$ 1,953,146**	$ 1,688,680
Accumulated other comprehensive income (loss) – net of taxes (note 9)		
Balance – end of year consists of:		
Net unrealized gains on available-for-sale assets	**$ 172,698**	$ –
Unrealized losses on translation of financial statement operations with US dollar functional currency to Canadian dollar reporting	**(78,216)**	(37,730)
Other comprehensive income of equity investment	**4,943**	–
Balance – end of year	**$ 99,425**	$ (37,730)

The accompanying notes constitute an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

	For the year ended December 31	
	2007	2006 (note 3)
	('000s)	
Net income for the year	**$ 115,776**	$ 167,100
Other comprehensive loss, net of taxes (note 9):		
Unrealized losses on available-for-sale assets	**(39,396)**	–
Reclassifications to net income for available-for-sale assets	**(72,406)**	–
Unrealized losses on translation of financial statement operations with US dollar functional currency to Canadian dollar reporting currency	**(40,486)**	(424)
Other comprehensive loss of equity investment	**(1,162)**	–
Total other comprehensive loss	**(153,450)**	(424)
Total comprehensive income (loss)	**$ (37,674)**	$ 166,676

The accompanying notes constitute an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

	For the year ended December 31	
	2007	2006 (note 3)
	('000s)	
Cash provided by (used in)		
Operating activities		
Receipts		
Premiums received	**$ 1,737,245**	$ 1,718,895
Investment income received	**173,617**	167,541
	1,910,862	1,886,436
Payments		
Claims paid, net of reinsurance recovered	**1,219,162**	1,060,331
Expenses paid	**460,368**	436,313
Income taxes paid	**139,548**	128,459
Change in other assets and liabilities	**(22,960)**	21,913
	1,796,118	1,647,016
Net cash from operating activities	**114,744**	239,420
Investing activities		
Bonds purchased	**(5,978,789)**	(5,238,178)
Bonds sold, redeemed or matured	**5,729,478**	5,044,734
Stocks purchased	**(270,632)**	(408,197)
Stocks sold or redeemed	**389,516**	255,374
Furniture and equipment, net	**(4,436)**	(4,931)
Real estate purchased	**(189)**	(809)
Other assets, net	**(2,401)**	1,784
Foreign exchange	**42,993**	(773)
Net cash used in investing activities	**(94,460)**	(350,996)
Increase (decrease) in cash for the year	**20,284**	(111,576)
Cash, cash equivalents and short-term deposits (bank indebtedness) – beginning of year	**(26,821)**	84,755
Bank indebtedness – end of year	**$ (6,537)**	$ (26,821)

The accompanying notes constitute an integral part of the consolidated financial statements.

1 REPORTING RESPONSIBILITIES

The financial statements and accompanying notes are the responsibility of management.

The external auditors of the Company are required to conduct an examination in accordance with Canadian generally accepted auditing standards to enable their reporting to the policyholders as to whether the annual financial statements present fairly, in all material respects, the financial position and results of operations of the Company in accordance with Canadian generally accepted accounting principles.

The Actuary is appointed by the Board of Directors pursuant to the Insurance Companies Act. He is responsible for ensuring that the assumptions and methods used in the valuation of policy liabilities are in accordance with accepted actuarial practice, applicable legislation and associated regulations or directives. He is also required to provide an opinion regarding the appropriateness of the policy liabilities at the balance sheet date to meet all policyholder obligations of the Company. Examination of supporting data for accuracy and completeness and analysis of Company assets for their ability to support the amount of policy liabilities are important elements of the work required to form this opinion.

Policy liabilities primarily include unearned premiums, unpaid claims and adjustment expenses, the reinsurers' share of unearned premiums and unpaid claims and adjustment expenses and deferred premium acquisition costs. The Appointed Actuary uses the work of the external and internal auditors in verifying data files for valuation purposes.

2 BASIS OF PRESENTATION

These financial statements have been prepared in accordance with the Insurance Companies Act which states that, except as otherwise specified by the Superintendent of Financial Institutions Canada ("the Superintendent"), the financial statements are to be prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The significant accounting policies used in the preparation of these financial statements are summarized in note 4. These accounting policies conform, in all material respects, to Canadian GAAP except that one subsidiary is not consolidated, as described below.

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as at the date of the financial statements and the reported amounts of revenue and expenses during the periods covered by the financial statements. The principal financial statement components subject to measurement uncertainty include the provision for unpaid claims (note 7) and the carrying value of future tax assets (note 9). Actual results could differ from those estimates.

3 CHANGE IN ACCOUNTING POLICIES

On January 1, 2007, the Company adopted the following new accounting standards that were issued by The Canadian Institute of Chartered Accountants (CICA): CICA Handbook Section 1530, "Comprehensive Income"; Section 3251, "Equity"; Section 3855, "Financial Instruments – Recognition and Measurement"; Section 3861, "Financial Instruments – Disclosure and Presentation"; and Section 3865, "Hedges". The adoption of these new standards resulted in changes in the accounting for financial instruments and the recognition of certain transitional adjustments that have been recorded in opening retained earnings and opening accumulated other comprehensive income, as described below. The Company adopted these standards at the beginning of the year and, in accordance with the transitional provisions, the prior period balances have not been restated, except for the presentation of the foreign currency translation account, which was adopted retroactively.

Section 1530 establishes standards for reporting and presenting comprehensive income. Comprehensive income comprises net income and other comprehensive income (OCI) and includes all changes in equity (net assets) of the Company. Changes in unrealized gains and losses on available-for-sale (AFS) investments and unrealized gains and losses on self-sustaining foreign operations are recorded in OCI and included in accumulated other comprehensive income (AOCI) until recognized in the statement of operations.

Section 3251 describes the changes in how to report and disclose equity and changes in equity as a result of the new requirements of Section 1530. Upon adoption of these standards, the Company has presented a consolidated statement of comprehensive income for changes in these items during the year. Cumulative changes in OCI are included in AOCI which is presented in a new statement called "Consolidated Statement of Equity".

Section 3855 establishes standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives. Under Section 3855, financial instruments must be classified as held for trading (HFT), held to maturity (HTM), loans and receivables, AFS financial assets or other financial liabilities. All financial instruments, including derivatives, are measured on the balance sheet at fair value, except for those classified as loans and receivables, HTM investments and other financial liabilities, which are initially recognized at fair value and subsequently are measured at amortized cost using the effective interest rate method. Changes in fair value of AFS financial assets are recorded in OCI until the investment is sold or impaired; at which time, the realized gain or loss will be recorded in net income.

Section 3861 establishes standards for the presentation of financial instruments and non-financial derivatives and identifies the related information that should be disclosed.

Section 3865 describes when and how hedge accounting can be applied. The Company does not have any hedging relationships.

On adoption of the new standards, as at January 1, 2007, the Company classified all of its investments as AFS. The adjustment to increase the carrying value of these investments from cost/amortized cost ($3,410,774,000) to fair value ($3,841,377,000) has been recorded as an opening adjustment to AOCI, net of income taxes of $146,103,000. In addition, a recovery of $5,715,000 was recorded to opening retained earnings to adjust the future income tax balance to the historical taxes paid on the fair value adjustments in AOCI. Receivables and due from Facility Association are classified as loans and receivables, while other liabilities, unearned premiums and mortgage payable are classified as other financial liabilities, all of which are measured at amortized cost. The difference between cost and amortized cost was not material and therefore, no adjustment was recorded. The cumulative foreign currency translation account of $37,730 previously recorded as a component of retained earnings was reclassified to AOCI.

The impact of recording the investments at fair value on the selection of the discount rate and the measurement of the unpaid claims was a reduction of $7,326,000 and has been recorded as an adjustment to opening retained earnings, net of income taxes of $2,427,000.

The impact of recording the new financial instrument standards at the subsidiary level resulted in an increase of $7,026,000 to the investment in subsidiary account and has been recorded as an opening adjustment to AOCI. This amount includes a recovery of $1,018,000 which has been recorded as an adjustment to opening retained earnings.

The Company is also required to identify and record separately on its balance sheet derivatives embedded in other financial instruments not classified as HFT (the host instrument). Prior to the adoption of this standard, such embedded derivatives were not accounted for separately from the host contract.

In accordance with Section 3855, the Company has chosen a transaction date of January 1, 2003. All contracts entered into before this date were not considered for the existence of embedded derivatives. The Company has determined that there were no embedded derivatives.

A summary of the impact on the balance sheet of adopting the new standards follows.

	As at December 31, 2006	Adjustment on adoption of new standards	As at January 1, 2007
		('000s)	
Bonds	$ 2,370,950	$ 19,865	$ 2,390,815
Preferred shares	41,446	3,145	44,591
Common shares	998,378	407,593	1,405,971
Investment in subsidiary	43,939	7,026	50,965
Future income tax asset	142,186	(142,815)	(629)
Unpaid claims	1,520,948	(7,326)	1,513,622
Retained earnings	1,688,680	49,265	1,737,945
Accumulated other comprehensive income	–	252,875	252,875

There was no impact on reported net income for the year ended December 31, 2006.

4 SIGNIFICANT ACCOUNTING POLICIES

Basis of consolidation

These financial statements include consolidation of the wholly-owned subsidiary, Wawanesa General Insurance Company. The wholly-owned subsidiary, The Wawanesa Life Insurance Company, is not consolidated because management of the Company has determined that reporting of property and casualty and life insurance operations on a consolidated basis would not provide meaningful presentation. The Wawanesa Life Insurance Company is accounted for by the equity method. Its income is reflected in operations and the cost of the investment is adjusted to include post-acquisition income and is reduced by dividends.

Premiums earned

Premiums are taken into income on a pro-rata basis over the policy term.

Investment income

Investment income is recorded as it accrues. Dividend income on common and preferred shares is recorded on the ex dividend date. Gains and losses are determined and recorded as at the trade date, and are calculated on the basis of average cost.

The effective interest rate method is used to amortize premiums or discounts on the purchase of AFS bonds.

Acquisition expenses

Commissions and premium taxes are deferred to the extent that they are considered recoverable and are expensed in the accounting periods in which related premiums are recognized as income. The ultimate recoverability of acquisition expenses is determined without regard to investment income.

Available-for-sale financial assets

AFS financial assets with quoted prices in an active market are carried at fair value on the balance sheet from the trade date. Changes in fair values are recorded, net of income taxes, in AOCI when the financial asset is disposed of or has become other than temporarily impaired. When the financial asset is disposed of or has been temporarily impaired, the accumulated fair value adjustments recognized in AOCI are transferred to the statement of operations. A provision for impairment for equity instruments and debt securities classified as AFS is established when there is objective evidence that the investment is impaired and the impairment is other than temporary. Equity investments that are classified as AFS and do not have a quoted price in an active market are recorded at cost.

Loans and receivables

Financial assets classified as loans and receivables are initially recognized at fair value and subsequently measured at amortized cost using the effective interest rate method.

Financial liabilities

Any such liabilities, other than unpaid claims, are initially recognized at fair value and subsequently measured at amortized cost using the effective interest rate method.

Foreign exchange translation

The Company translates the assets, liabilities, income and expenses of its United States branch and its United States subsidiary, both of which are self-sustaining operations, to Canadian dollars on the following basis:

- Assets and liabilities are translated at the rate of exchange in effect at the balance sheet date.
- Income and expense items are translated at the rate in effect on the dates they occur.
- Gains and losses resulting from translation are deferred and shown as a separate component of accumulated other comprehensive income (loss).

Income taxes

Future income taxes result from temporary differences in the tax basis of an asset or liability and its carrying amount in the balance sheet. The future income tax asset/liability is computed at the tax rates that are expected to apply when the income tax asset or liability is settled.

Employee future benefits

The Company maintains defined benefit plans for substantially all employees. The plans provide pensions based on length of service and final average earnings. In addition, the Company provides life insurance, dental and health benefit plans for retired employees.

The costs of these benefits related to current service are charged to operations in the period in which the services are rendered. The actuarial determination of the accrued benefit obligations uses the projected benefit method prorated on service (which incorporates management's best estimate of future salary levels, future cost escalation, retirement ages of employees and other actuarial factors). Past service costs, any net excess actuarial gains or losses over 10% of the greater of the accrued benefit obligation and the market value of the plans assets, together with the transitional assets that resulted on the adoption of the new accounting standards, are amortized over the expected average remaining service lives of the employee group.

The excess of funding pension payments over pension expense is recorded as an asset. Non-pension benefits are not funded. The accumulated non-pension benefit expense is recorded as a liability.

The Company also provides defined contribution plans for certain employees. Contributions are expensed in the period that they are paid.

Unpaid claims

The provision for unpaid claims is established by the case method as claims are reported. The estimates are regularly reviewed and updated as additional information on the estimated unpaid claims becomes known and any resulting adjustments are included in the statement of operations. A provision is also made for management's calculation of factors affecting future development of unpaid claims including claims incurred but not reported (IBNR) based on the volume of business currently in force and the historical experience on claims. The unpaid claims are discounted as mandated by the Superintendent.

Salvage and subrogation

Salvage and subrogation recoveries on claims are recorded as a reduction of claims incurred on an accrual basis.

5 INVESTMENTS AND RELATED NET INVESTMENT INCOME

a) Fair value of investments

	2007	2006
	('000s)	
Bonds		
Canadian	**$ 1,748,590**	$ 1,672,665
American	**772,268**	718,150
	2,520,858	2,390,815
Stocks		
Preferred		
Canadian	**45,917**	44,591
Common		
Canadian	**616,914**	682,965
Foreign	**637,306**	723,006
	1,300,137	1,450,562
Total investments	**$ 3,820,995**	$ 3,841,377

b) Bonds

The fair value of publicly traded bonds is determined using quoted market bid prices. For non-publicly traded bonds, fair value is determined using a discounted cash flow approach that includes provisions for credit risk and the expected maturities of the securities. The valuation techniques used are primarily based on observable market prices or rates. In limited circumstances, valuation assumptions not based on observable market data may be used. The Company does not believe that using alternative assumptions in the valuation techniques for these bonds would result in significantly different fair values.

Available-for-sale bonds are reported at fair value on the balance sheet. Therefore, the carrying value of these bonds is equal to their fair value.

c) Stocks

The fair value of publicly traded stocks is determined using quoted market bid prices.

Available-for-sale stocks are reported at fair value on the balance sheet. For these stocks, the carrying value is equal to their fair value. Stocks that do not have a quoted market price on an active market are reported at cost and are not material to these financial statements.

d) Temporarily impaired available-for-sale assets

The available-for-sale assets disclosed in the following table exhibit evidence of impairment, however, the impairment loss has not been recognized in net income because it is considered temporary. Available-for-sale bonds and stocks have generally been identified as temporarily impaired if their amortized cost as at December 31, 2007 was greater than their fair value, resulting in an unrealized loss. Unrealized losses may be due to interest rate fluctuations and/or depressed fair values in sectors which have experienced unusually strong negative market reactions. In connection with the Company's investment management practices and review of its investment holdings, it is believed that the contractual terms of bond investments will be met and/or the Company has the ability to hold these investments until recovery in value.

	Fair value	Unrealized losses
	('000s)	
Available-for-sale bonds	$ 1,199,316	$ 32,730
Available-for-sale stocks	308,033	39,470
Total temporarily impaired financial assets	$ 1,507,349	$ 72,200

Included in realized gains on sale of available-for-sale assets is write-downs of available-for-sale financial assets due to other-than-temporary impairment of $7,720,000 for the year ended December 31, 2007. Write-downs of $214,000 were included in realized gains on sale of investments for the year ended December 31, 2006.

e) Other net investment income

Other net investment income has the following components:

	2007	2006
	('000s)	
Interest income		
Bonds	**$ –**	$ 106,743
Available-for-sale bonds	**116,887**	–
Cash, cash equivalents and short-term securities	**3,084**	6,358
Dividends from stocks	**–**	15,912
Dividends on available-for-sale stocks	**21,066**	–
Other income	**20,979**	16,330
Investment expenses	**(4,719)**	(4,643)
Interest expense	**(13,140)**	(934)
Total other net investment income and management fees	**$ 144,157**	$ 139,766

Included in interest expense is $11,900,000 estimated exposure related to a Canada Revenue Agency ("CRA") audit (note 9).

Financial risk management objectives and policies

Investment risk management is carried out by an investment committee under policies approved by the Board of Directors. The Company has written principles for overall risk management, as well as written policies covering specific areas, such as underwriting, reinsurance, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments and investment of excess liquidity.

Credit risk: The Company is exposed to credit risk principally through its investment securities and balances receivable from policyholders and reinsurers. The Company has policies to limit and monitor its exposure to individual issuers and classes of issuers of investment securities which do not carry the guarantee of a national or Canadian provincial government. The Company's credit exposure to any one individual policyholder is not material. The Company monitors its exposure to brokers and has procedures to ensure that it works only with licensed firms in good standing with their regulatory bodies. The Company limits its exposure to individual reinsurers and regularly reviews the creditworthiness of reinsurers with whom it transacts business.

Equity price risk: The Company has policies to limit and monitor its exposure to individual issuers and industry sectors.

6 INVESTMENT IN SUBSIDIARY

	2007	2006
	('000s)	
The Wawanesa Life Insurance Company, 100% owned	**$ 54,365**	$ 43,939

A summary of the significant balance sheet items for The Wawanesa Life Insurance Company is as follows:

	2007	2006
	('000s)	
Investments	**$ 481,071**	$ 435,382
Accrued investment income	**3,885**	3,858
Other assets	**11,748**	7,423
	$ 496,704	$ 446,663
Policy liabilities	**$ 394,819**	$ 350,255
Other liabilities	**10,196**	20,205
Total equity	**91,689**	76,203
	$ 496,704	$ 446,663

A summary of the significant operating results for The Wawanesa Life Insurance Company is as follows:

	2007	2006
	('000s)	
Premium income	**$ 85,870**	$ 80,721
Net investment income	**17,267**	26,459
	103,137	107,180
Benefits and expenses	**93,615**	98,928
Income before income taxes	**9,522**	8,252
Income taxes	**2,220**	2,429
Net income for the year	**7,302**	5,823
Other comprehensive loss for the year	**(2,441)**	–
Total comprehensive income for the year	**$ 4,861**	$ 5,823

7 UNPAID CLAIMS

Management believes that the unpaid claims provision is appropriately established in the aggregate and is adequate to cover the ultimate net cost on a discounted basis. The determination of this provision, which includes unpaid claims, adjustment expenses, expected salvage and subrogation and the related reinsurers' share of each requires an assessment of future claims development. This assessment takes into account the consistency of the Company's claim handling procedures, the amount of information available, the characteristics of the line of business from which the claims arise and the delay inherent in claims reporting. This provision is an estimate and as such is subject to variability that may arise from future events, such as the receipt of additional claims information, changes in judicial interpretation of contracts or significant changes in frequency and severity of claims. This estimate is principally based on the Company's historical experience and may be revised as additional experience becomes available. Any such changes would be reflected in the statement of operations for the period in which the change occurred. This estimate does reflect the time value of money as mandated by the Superintendent. In that respect, the Company determines the discount rate based upon the expected return of bonds held in the portfolio that approximates the cash flow requirements of the unpaid claim. The discount rate applied was 5.25% (2006 – 4.75%). To recognize the uncertainty inherent in determining unpaid claim amounts, the Company includes a Provision for Adverse Deviations (PFADs) relating to claim development, reinsurance recoveries and future investment income. The PFADs selected are all within the ranges recommended by the Canadian Institute of Actuaries.

The table below details the provision for unpaid claims by major line of business:

	2007	2006
	('000s)	
Line of business		
Automobile	**$ 1,287,845**	$ 1,220,208
Personal property	**255,532**	190,440
Commercial property	**95,536**	75,435
Other	**39,547**	34,865
Total gross unpaid claims	**1,678,460**	1,520,948
Reinsurers' portion	**31,620**	3,220
Net unpaid claims	**$ 1,646,840**	$ 1,517,728

Changes in unpaid claims:

	2007	2006
	('000s)	
Unpaid claims – beginning of year – as previously reported	**$ 1,520,948**	$ 1,394,637
Adjustment for change in accounting policy (note 3)	**(7,326)**	–
Unpaid claims – beginning of year – after change in accounting policy	**1,513,622**	1,394,637
Change in estimates for losses occurring in prior years	**(30,365)**	(16,418)
Provision for claims occurring in the current year	**1,403,535**	1,234,658
Paid on claims	**(1,208,332)**	(1,091,929)
Unpaid claims – end of year	**$ 1,678,460**	$ 1,520,948

Effects of discounting on unpaid claims and adjustment expenses:

	Undiscounted	Effects of present value	PFAD	Discounted
2007		('000s)		
Provision for unpaid claims and adjustment expenses	**$ 1,717,811**	**$ (184,450)**	**$ 145,099**	**$ 1,678,460**
Reinsurers' share of unpaid claims	**31,821**	**(1,568)**	**1,367**	**31,620**
	$ 1,685,990	**$ (182,882)**	**$ 143,732**	**$ 1,646,840**
2006				
Provision for unpaid claims and adjustment expenses	$ 1,544,265	$ (156,560)	$ 133,243	$ 1,520,948
Reinsurers' share of unpaid claims	3,392	(649)	477	3,220
	$ 1,540,873	$ (155,911)	$ 132,766	$ 1,517,728

8 EMPLOYEE FUTURE BENEFITS

Description of benefit plans

The Company has a number of defined benefit and defined contribution plans providing pension and other retirement benefits to most of its employees. Pension benefits are based on length of service and final average earnings and may be indexed at the discretion of the Board of Directors. Other retirement benefit plans are non-contributory health care and life insurance plans.

Total cash payments

Total cash payments for employee future benefits for 2007, consisting of cash contributed by the Company to its funded pension plans, cash payments directly to beneficiaries for unfunded other benefit plans, and cash contributed to defined contribution plans, was $12,928,000 (2006 – $11,001,000).

Defined benefit plans

The Company measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at December 31 of each year. The most recent actuarial valuation of the defined benefit pension plan and the supplemental plan for funding purposes was as of December 31, 2006. The next required valuation of the supplemental plan and the defined benefit pension plan will be December 31, 2007 and December 31, 2009, respectively.

Defined benefit plan assets

The percentage of plan assets by major category measured at December 31 is:

	2007	2006
	%	%
Equity securities	**62**	63
Debt securities	**33**	34
Other	**5**	3
	100	100

Reconciliation of the funded status of the benefit plans to the amounts recorded in the financial statements

	Pension benefit plans		Other benefit plans	
	2007	2006	2007	2006
	('000s)		('000s)	
Market value of plan assets	**$ 277,445**	$ 274,827	**$ –**	$ –
Accrued benefit obligation	**(287,233)**	(256,816)	**(38,868)**	(32,445)
Funded status of plans – surplus (deficit)	**(9,788)**	18,011	**(38,868)**	(32,445)
Balance of unamortized (gains) losses	**22,654**	(7,307)	**14,488**	10,845
Accrued benefit asset (liability)	**$ 12,866**	$ 10,704	**$ (24,380)**	$ (21,600)

The accrued benefit asset (liability) is included in the Company's balance sheet as follows:

	Pension benefit plans		Other benefit plans	
	2007	2006	2007	2006
	('000s)		('000s)	
Receivables	**$ 12,866**	$ 10,704	**$ –**	$ –
Other liabilities	**–**	–	**(24,380)**	(21,600)
	$ 12,866	$ 10,704	**$ (24,380)**	$ (21,600)

Plans with accrued benefit obligations in excess of plan assets

Included in the above accrued benefit obligation and fair value of plan assets at year end are the following amounts in respect of plans that are not fully funded:

	Pension benefit plans		Other benefit plans	
	2007	2006	2007	2006
	('000s)		('000s)	
Accrued benefit obligation	**$ (287,233)**	$ (20,672)	**$ (38,868)**	$ (32,445)
Fair value of plan assets	**277,445**	18,113	**–**	–
Funded status – plan deficit	**$ (9,788)**	$ (2,559)	**$ (38,868)**	$ (32,445)

Significant assumptions

The significant weighted average assumptions used in measuring the Company's pension and other obligations as at December 31 are:

	Pension benefit plans		Other benefit plans	
	2007	2006	2007	2006
Accrued benefit obligation:				
Discount rate	**4.75%**	4.75%	**5.45%**	5.25%
Rate of compensation increase	**4.90%**	4.75%	**–**	–
Benefit costs:				
Discount rate	**4.75%**	4.75%	**5.25%**	5.25%
Expected long-term rate of return on plan assets	**4.68%**	4.68%	**–**	–
Rate of compensation increase	**4.90%**	4.75%	**–**	–
Assumed health care cost trend rates*	**–**	–	**8.00%**	9.00%

* The health care cost trend rate will decline by 1% per year to the ultimate rate of 5% in 2010.

Benefits paid

Benefits paid were as follows:

	2007	2006
	('000s)	
Plans providing pension benefits	**$ 8,552**	$ 5,899
Plans providing other benefits	**678**	484
	$ 9,230	$ 6,383

Employee future benefit costs recognized in the year

The total cost recognized for the Company's defined benefit plans is as follows:

	2007	2006
	('000s)	
Plans providing pension benefits	**$ 9,113**	$ 8,897
Plans providing other benefits	**3,536**	3,592
	$ 12,649	$ 12,489

Defined contribution plans

The total cost recognized for the Company's defined contribution plans is as follows:

	2007	2006
	('000s)	
Plans providing pension benefits	**$ 474**	$ 413

9 INCOME TAXES

The provision for income taxes reflects an effective tax rate that differs from the combined tax rate for Canadian federal and provincial corporate taxes for the following:

	2007	2006
	('000s)	
Earnings before income taxes	**$ 175,388**	$ 257,801
Combined statutory tax rate	**34.14%**	34.60%
Tax payable based on statutory tax rate	**59,877**	89,199
Effect of:		
Permanent differences	**(3,017)**	(5,993)
Future income tax rate changes	**(4,008)**	7,875
Provision for uncertain tax filing positions	**700**	10,335
Adjustment to future tax liability	**8,476**	–
Realization of future tax asset previously not recorded	**–**	(10,612)
Capital taxes	**148**	137
Other	**1,998**	2,190
	$ 64,174	$ 93,131
Provision for income taxes		
Current	**$ 58,143**	$ 126,172
Future	**6,031**	(33,041)
	$ 64,174	$ 93,131

As a result of the ongoing CRA tax audit of the fiscal years 2003 to 2005, a net adjustment in the amount of $700,000 (2006 – $13,000,000) has been recorded as tax expense in the provision for uncertain tax filing positions. Interest expense related to this exposure of $11,900,000 has been recorded as a reduction to investment income in the current year.

The Company has also recorded an additional $8,476,000 future tax expense to recognize the future tax liability associated with the Company's tax filing position related to the earthquake premium reserve deduction.

Future income tax assets and liabilities consist of temporary differences between the accounting and tax basis of assets and liabilities as follows:

	2007	2006
	('000s)	
Future income tax assets		
Invested assets	**$ (11,446)**	$ 97,844
Policy liabilities and other policy reserves	**20,140**	35,947
Employee future benefits	**3,783**	3,661
Other assets	**3,742**	4,734
	$ 16,219	$ 142,186

The Company expects that future income assets will be realized in the normal course of operations.

Income taxes included in OCI

Other comprehensive income included on the statement of comprehensive income is presented net of income taxes. The following income tax amounts are included in each component of other comprehensive income for the year ended December 31:

	2007	2006
	('000s)	
Unrealized losses on available-for-sale assets	**$ 11,460**	$ –
Reclassifications to net income for available-for-sale assets	**37,585**	–
Unrealized losses on translation of financial statement operations with US dollar functional currency to Canadian dollar reporting currency	**10,293**	776
Other comprehensive income of equity investment	**1,307**	–
Total income taxes recovery included in OCI	**$ 60,645**	$ 776

10 MORTGAGE PAYABLE

The mortgage payment due in 2008, including principle and interest, of $13,781,108 to Standard Life Assurance Company is due December 1, 2008, payable in monthly instalments of $87,887 including interest at 6.75% and is secured by land and building, an assignment of leases and chattels therein.

The mortgage was assumed as part of the vendor's terms on the acquisition of an office building in Winnipeg.

11 REINSURANCE

The Company had reinsurance in force during the year to limit its liability as follows:

- In the event of a series of claims arising out of a single occurrence the Company had obtained reinsurance with an upper amount of $450,000,000, which limited its liability to $36,375,000 in the event of a series of claims arising out of a single occurrence.
- Aggregate protection up to $25,000,000 after satisfaction of a $35,000,000 deductible. This deductible is based on an accumulation of all losses subject to the treaty that exceed $2,500,000 and are less than $22,500,000.

	2007	2006
	('000s)	
Net premiums ceded on an earned basis	**$ 35,745**	$ 36,163
Net claims and adjustment expenses ceded	**32,115**	3,066

Reinsurance recoverables

In the normal course of business, the Company limits the amount of loss on any one policy by reinsuring certain levels of risk in various areas of exposure with reinsurers.

Reinsurance ceded does not discharge the Company's liability as the primary insurer. Failure of reinsurers to honour their obligations could result in losses to the Company. A contingent liability exists should an assuming company be unable to meet its obligations.

At December 31, 2007, the Company had outstanding balances from reinsurers of $16,957,000. All amounts are with reinsurers with a credit rating of A.

12 CONTINGENT LIABILITIES

The Company has settled some claims by purchasing annuities (structured settlements) from life insurers. The Company guarantees the future annuity payments and thus is exposed to a credit risk to the extent any of the life insurers fail to fulfill their obligations. The risk is managed by acquiring annuities from several Canadian life insurers with proven financial stability. To December 31, 2007, no information has come to the Company's attention to suggest any financial weakness in life insurers from which it has purchased annuities. Consequently, no provision for credit risk is required. The credit risk exposure is estimated at the original purchase price of the annuities of $74,221,000 (2006 – $68,126,000).

13 RELATED PARTY TRANSACTIONS

The Company has the following transactions with its wholly-owned subsidiary, The Wawanesa Life Insurance Company:

- The Company recovers the cost of expenses paid on behalf of or shared with the subsidiary totalling $11,057,000 (2006 – $10,412,000).
- The Company pays commissions on behalf of its brokers to investment accounts maintained by the subsidiary of $9,039,000 (2006 – $8,399,000).
- The Company purchases group employee benefits from the subsidiary at a cost of $4,594,000 (2006 – $3,674,000).

Balances between the Company and its subsidiary are settled on a regular basis and the outstanding amounts are immaterial at December 31, 2007 and 2006.

14 PREMIUM RATE REGULATION

Substantially all of the Company's automobile business and its United States property business are subject to rate regulation by various provincial and state regulators. This business comprises approximately 65% (2006 – 67%) of gross premiums written.

Regulation of premium rates is based on the cost of providing insurance coverage which recognizes claims and other costs including anticipated profit margins. Insurance premiums can be subject to mandatory rate rollbacks and mandatory rate assessments imposed by provincial or state legislation or regulation. This could result in lower future premium rates or reductions to premium rates charged by the Company in prior periods. In addition, the Company is required, under the legislation of certain jurisdictions, to participate in risk sharing pools which may impact positively or negatively upon underwriting results. The impact of the participation is immaterial to the overall financial statements.

At various points throughout the year the Company will have applications pending with certain regulators for automobile premium rate changes. All are in the normal course of business. The Company is not aware of any proposed or pending rate rollbacks related to prior years.

15 FUTURE IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

Capital disclosures and financial instruments – disclosure and presentation

On January 1, 2008, the Company will adopt three new CICA Handbook Sections: Section 1535, "Capital Disclosures", Section 3862, "Financial Instruments – Disclosures", and Section 3863, "Financial Instruments – Presentation". Section 1535 requires disclosure of an entity's objectives, policies and processes for managing capital; information about what the entity regards as capital; whether the entity has complied with any capital requirements; and the consequences of not complying with these capital requirements. Sections 3862 and 3863 replace Handbook Section 3861, "Financial Instruments – Disclosure and Presentation". Section 3863 carries forward unchanged the presentation requirements of Section 3861 while Section 3862 requires enhanced financial instrument disclosures focusing on disclosures related to the nature and extent of risks arising from financial instruments and how the entity manages those risks. The Company will apply the new disclosures in its 2008 financial statements.

16 COMPARATIVE FIGURES

Certain of the prior year's figures have been restated for comparative purposes.

17 SUBSEQUENT EVENTS

On February 8, 2008, the Alberta Court of Queen's Bench ruled that the Minor Injury Regulation should be struck down as it is inconsistent with the Constitution Act 1982 in that it discriminated on a basis of a prohibited enumerated ground under Section 15 of the Charter, namely, physical disability.

The Minor Injury Regulation was introduced on October 1, 2004 as part of a comprehensive automobile insurance reform package in the Province of Alberta. It capped minor soft-tissue general damage payments at $4,000. This ruling will impact all open minor soft-tissue claims and potentially any claims that occurred after October 1, 2004 which have been subsequently closed.

The Government has indicated its intention to appeal the decision.

The Company has determined that there is considerable uncertainty concerning the ultimate outcome of this situation. However, the Appointed Actuary has estimated the potential exposure to the Company under various scenarios and probabilities. Based on this estimation, the Appointed Actuary has determined that the unpaid claims provision currently recorded in the financial statements provides a reasonable provision to cover this potential exposure.

Incorporated July 7, 1960

Head Office
Wawanesa, Manitoba

Executive Office
200 – 191 Broadway
Winnipeg, Manitoba

OFFICERS AND MANAGEMENT

Corporate

K. E. McCrea, CA, FLMI
President and Chief Executive Officer

M. K. Nemeth, CA, FLMI, GBA
Vice President and Chief Operating Officer

G. N. Bass, Q.C.
Vice President, General Counsel and Secretary

I. R. MacDonald, FSA, FCIA
Vice President and Actuary

C. R. Loeppky, BScCS
Vice President, Information Services

T. L. Nelson, FLMI/M, CHRP, CIP
Vice President, Human Resources

W. D. Evans
Manager, Residential Mortgages

P. M. Horncastle, CGA
Comptroller

P. R. Mulaire, CMA, FCIP, CIA
Manager, Internal Audit

K. J. Richtik, FSA, FCIA
Manager, Actuarial Financial Reporting

Insurance Operations

G. G. Sadler, CLU, ChFC, RHU
Director, Individual Sales and Marketing

R. A. Maharajh, CMA, FSA, FCIA
Group Actuary

M. M. Nolin, ALHC
Manager, Group Claims

D. M. Smook
Manager, National Group Sales & Service

A. E. Waller, MBA, CFP, ChFC, CLU
Manager, Individual Life Administration

Medical Director

Dr. R. B. Boyd, MD

To the Policyholders and Shareholder of The Wawanesa Life Insurance Company

We have audited the balance sheet of **The Wawanesa Life Insurance Company** as at December 31, 2007 and the statements of operations, comprehensive income, equity, cash flows, changes in segregated funds net assets and segregated funds net assets for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants
February 27, 2008, Winnipeg, Manitoba

To the Policyholders and Shareholder of The Wawanesa Life Insurance Company

I have valued the policy liabilities of **The Wawanesa Life Insurance Company** for its balance sheet at December 31, 2007 and their change in the statement of operations for the year then ended in accordance with accepted actuarial practice, including selection of appropriate assumptions and methods.

In my opinion, the amount of policy liabilities makes appropriate provision for all policyholder obligations and the financial statements fairly present the result of the valuation.

Ian R. MacDonald

Ian R. MacDonald, FSA, FCIA
Fellow, Canadian Institute of Actuaries
February 27, 2008, Winnipeg, Manitoba

BRANCH OFFICES

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J. C. Best
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Individual Life Manager

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R. W. Bridle
Individual Life Manager

B. I. Lang, RHU
Individual Life Manager

E. T. Tollefsen
Regional Group Manager

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Brandon, Manitoba

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Individual Life Manager

Saskatchewan, Eastern Manitoba and NW Ontario
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Calgary, Alberta

C. R. Stauffer
Individual Life Manager

British Columbia
310 – 1985 West Broadway
Vancouver, British Columbia

B. L. Russell
Individual Life Manager

S. F. Engmann
Individual Life Manager

T. C. Hickmore, GBA
Regional Group Manager

B. R. Wyne, MBA
Regional Group Manager

BALANCE SHEET

	As at December 31	
	2007	2006 (note 3)
	('000s)	
Assets		
Investments (note 5)	**$ 481,071**	$ 435,382
Cash	**6,578**	1,780
Outstanding premiums	**525**	863
Investment income due and accrued	**3,885**	3,858
Income taxes recoverable	**1,809**	1,191
Other assets	**2,836**	3,522
Total general fund assets	**$ 496,704**	$ 446,596
Segregated funds net assets (note 9)	**$ 140,321**	$ 129,104
Liabilities		
Policy liabilities (note 6)	**$ 394,819**	$ 350,255
Other liabilities	**2,438**	2,067
Future income taxes (note 8)	**7,758**	1,893
Deferred gains on disposal of portfolio investments (note 3)	**–**	16,178
Total general fund liabilities	**405,015**	370,393
Total equity	**91,689**	76,203
Total general fund liabilities and equity	**$ 496,704**	$ 446,596
Segregated fund contract liabilities	**$ 140,321**	$ 129,104

The accompanying notes constitute an integral part of the consolidated financial statements.

	For the year ended December 31	
	2007	2006 (note 3)
	('000s)	
Income		
Premiums		
Life insurance	$ 37,190	$ 34,725
Health insurance	19,610	20,179
Annuities	29,070	25,817
	85,870	80,721
Net investment income		
Change in fair value of held-for-trading assets	(7,941)	–
Realized gains on sales of available-for-sale assets	2,428	–
Other net investment income (note 5)	22,780	26,459
	103,137	107,180
Benefits and expenses		
Amounts paid or credited to policyholders and their beneficiaries		
Death, disability and health benefits	25,758	23,831
Annuity payments	4,003	4,000
Maturities and surrenders	27,826	26,342
Dividends and interest	4,710	4,305
Increase in actuarial liabilities	8,861	20,227
	71,158	78,705
Commissions	8,511	7,277
Operating expenses	12,304	11,333
Taxes and licences	1,642	1,613
	93,615	98,928
Income before income taxes	9,522	8,252
Income taxes (note 8)		
Current	34	1,346
Future	2,186	1,083
	2,220	2,429
Net income for the year	$ 7,302	$ 5,823

The accompanying notes constitute an integral part of the consolidated financial statements.

STATEMENT OF COMPREHENSIVE INCOME

	For the year ended December 31	
	2007	2006 (note 3)
	('000s)	
Net income for the year	**$ 7,302**	$ 5,823
Other comprehensive loss – net of taxes (note 8)		
Change in unrealized gains (losses) on available-for-sale assets	**(778)**	–
Reclassifications to net income for available-for-sale assets	**(1,663)**	–
Total other comprehensive loss	**(2,441)**	–
Total comprehensive income	**$ 4,861**	$ 5,823
Allocation of net income		
Participating policyholders' account	**$ 2,845**	$ 3,481
Shareholder account	**4,457**	2,342
Allocation of other comprehensive loss		
Participating policyholders' account	**(1,279)**	–
Shareholder account	**(1,162)**	–
	$ 4,861	$ 5,823

The accompanying notes constitute an integral part of the consolidated financial statements.

STATEMENT OF EQUITY

	For the year ended December 31			
	2007			2006 (note 3)
	Participating policyholders	Shareholder	Total	Total
	('000s)			
Share capital (note 10)	$ –	$ 11,500	$ 11,500	$ 11,500
Policyholders' account/retained earnings				
Balance – beginning of year, as previously reported	26,543	38,160	64,703	58,880
Adjustment for change in accounting policy (note 3)	199	920	1,119	–
Balance after change in accounting policy	26,742	39,080	65,822	58,880
Net income	2,845	4,457	7,302	5,823
Transfer (note 11)	(105)	105	–	–
Balance – end of year	29,482	43,642	73,124	64,703
Accumulated other comprehensive income (loss) – net of taxes (note 8)				
Balance – beginning of year, as a result of change in accounting policy (note 3)	3,400	6,106	9,506	–
Total other comprehensive loss	(1,279)	(1,162)	(2,441)	–
Balance – end of year	2,121	4,944	7,065	–
Total retained earnings and accumulated other comprehensive income	31,603	48,586	80,189	64,703
Total equity	$ 31,603	$ 60,086	91,689	76,203
Accumulated other comprehensive income – net of taxes (note 8)				
Balance – end of year consists of:				
Net unrealized gains on available-for-sale assets	$ 2,121	$ 4,944	$ 7,065	$ –
Balance – end of year	$ 2,121	$ 4,944	$ 7,065	$ –

The accompanying notes constitute an integral part of the consolidated financial statements.

STATEMENT OF CASH FLOWS

	For the year ended December 31	
	2007	2006 (note 3)
	('000s)	
Cash provided by (used in)		
Operating activities		
Receipts		
Premium and annuity considerations	**$ 83,750**	$ 78,174
Investment income received	**24,234**	20,335
Other revenue	**2,527**	2,134
	110,511	100,643
Payments		
Benefits and annuity payments	**50,508**	46,689
Net transfers to segregated funds	**7,675**	6,172
Insurance expenses and taxes	**22,752**	23,186
Dividends to policyholders	**4,710**	4,305
Change in other assets and liabilities	**(867)**	885
	84,778	81,237
Cash provided by operating activities	**25,733**	19,406
Investing activities		
Purchases, bonds and stocks	**(284,287)**	(256,974)
Disposals, bonds and stocks	**263,058**	243,301
Advances, mortgage and policy loans	**(10,396)**	(12,707)
Repayments, mortgage and policy loans	**10,690**	7,857
Cash used in investing activities	**(20,935)**	(18,523)
Increase in cash for the year	**4,798**	883
Cash – beginning of year	**1,780**	897
Cash – end of year	**$ 6,578**	$ 1,780
Income taxes paid	**$ 600**	$ 3,351

The accompanying notes constitute an integral part of the consolidated financial statements.

STATEMENT OF CHANGES IN SEGREGATED FUNDS NET ASSETS

	For the year ended December 31	
	2007	2006
	('000s)	
Additions to segregated funds		
Proceeds from sale of units	**$ 27,877**	$ 22,558
Unrealized appreciation (depreciation) of investments	**(1,461)**	13,440
Net realized gains	**4,136**	2,105
Investment income	**3,258**	2,691
	33,810	40,794
Deductions from segregated funds		
Payments on redemption of units	**20,203**	16,386
Management fees	**2,390**	2,020
	22,593	18,406
Net additions to segregated funds for the year	**11,217**	22,388
Segregated funds net assets – beginning of year	**129,104**	106,716
Segregated funds net assets – end of year	**$ 140,321**	$ 129,104

STATEMENT OF SEGREGATED FUNDS NET ASSETS

	As at December 31	
	2007	2006
	('000s)	
Assets		
Mutual Fund units	**$ 140,383**	$ 129,107
Liabilities		
Amounts due to The Wawanesa Life Insurance Company	**62**	3
Net assets attributed to segregated funds policyholders	**$ 140,321**	$ 129,104

The accompanying notes constitute an integral part of the consolidated financial statements.

1 REPORTING RESPONSIBILITIES

The financial statements and accompanying notes are the responsibility of management.

The external auditors of the Company are required to conduct an examination in accordance with Canadian generally accepted auditing standards to enable their reporting to the policyholders and shareholder as to whether the annual financial statements present fairly, in all material respects, the financial position and results of operations of the Company in accordance with Canadian generally accepted accounting principles.

The Actuary is appointed by the Board of Directors pursuant to the Insurance Companies Act. He is responsible for ensuring that the assumptions and methods used in the valuation of policy liabilities are in accordance with accepted actuarial practice, applicable legislation and associated regulations or directives. He is also required to provide an opinion regarding the appropriateness of the policy liabilities at the balance sheet date to meet all policyholder obligations of the Company. Examination of supporting data for accuracy and completeness and analysis of Company assets for their ability to support the amount of policy liabilities are important elements of the work required to form this opinion.

The Appointed Actuary uses the work of the external and internal auditors in verifying data files for valuation purposes.

2 BASIS OF PRESENTATION

The Wawanesa Life Insurance Company (referred to as the "Company") is a wholly-owned subsidiary of The Wawanesa Mutual Insurance Company. These financial statements have been prepared in accordance with the Insurance Companies Act which states that, except as otherwise specified by the Office of the Superintendent of Financial Institutions Canada (OSFI or the Superintendent), the financial statements are to be prepared in accordance with Canadian generally accepted accounting principles (GAAP). The significant accounting policies used in the preparation of these financial statements, including the accounting requirements of the Superintendent, are summarized below. These accounting policies conform, in all material respects, to Canadian generally accepted accounting principles.

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as at the date of the financial statements and the reported amounts of revenue and expenses during the periods covered by the financial statements. The principal financial statement components subject to measurement uncertainty include the provision for policy liabilities (note 6) and the carrying value of future tax liabilities (note 8). Actual results could differ from those estimates.

3 CHANGE IN ACCOUNTING POLICIES

Summary

On January 1, 2007, the Company adopted the following new accounting standards that were issued by The Canadian Institute of Chartered Accountants (CICA): Handbook Section 1530, "Comprehensive Income"; Section 3251, "Equity"; Section 3855, "Financial Instruments – Recognition and Measurement"; Section 3861, "Financial Instruments – Disclosure and Presentation"; Section 3865, "Hedges"; and Section 4211, "Life Insurance Enterprises – Specific Items".

The adoption of these new standards resulted in changes in the accounting for financial instruments and the recognition of certain transitional adjustments that have been recorded in opening retained earnings and opening accumulated other comprehensive income, as described below. The Company adopted these standards at the beginning of the year and, in accordance with the transitional provisions, the prior period balances have not been restated.

Section 1530 establishes standards for reporting and presenting comprehensive income. Comprehensive income comprises net income and other comprehensive income (OCI) and includes all changes in equity of the Company. Changes in unrealized gains and losses on available-for-sale (AFS) investments are recorded in OCI and included in accumulated other comprehensive income (AOCI) until recognized in the statement of operations.

Section 3251 describes the changes in how to report and disclose equity and changes in equity as a result of the new requirements of Section 1530. Upon adoption of these standards, the Company has presented a statement of comprehensive income for changes in these items during the year. Cumulative changes in OCI are included in AOCI which is presented in a new statement called "Statement of Equity".

Section 3855 establishes standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives. Under Section 3855, financial instruments must be classified as held for trading (HFT), held to maturity (HTM), loans and receivables, AFS financial assets or other financial liabilities. All financial instruments, including derivatives, are measured on the balance sheet at fair value, except for those classified as loans and receivables, HTM investments and other financial liabilities, which are initially recognized at fair value and subsequently are measured at amortized cost using the effective interest rate method. Changes in fair value of HFT financial instruments are recorded in net income. Changes in fair value of AFS financial assets are recorded in OCI until the investment is sold or impaired, at which time the realized gain or loss is recorded in net income.

Section 3861 establishes standards for the presentation of financial instruments and non-financial derivatives and identifies the related information that should be disclosed.

Section 3865 describes when and how hedge accounting can be applied. The Company does not have any hedging relationships.

The Company is also required to identify and record separately on its balance sheet derivatives embedded in other financial instruments not classified as HFT (the host instrument). Prior to the adoption of this standard, such embedded derivatives were not accounted for separately from the host contract.

The Company has determined that there were no embedded derivatives. In accordance with Section 3855, the Company has chosen a transaction date of January 1, 2003. All contracts entered into before this date were not considered for the existence of embedded derivatives.

Also effective January 1, 2007, CICA Handbook Section 4211, Life Insurance Enterprises – Specific Items, replaced CICA Handbook Section 4210. Financial assets previously included as portfolio investments are required to follow the accounting requirements in the new Handbook Sections 3855 and 1530. As a result, realized gains and losses on financial instruments no longer covered by Section 4211 are not deferred and amortized into income but are recognized in net income as fair value changes for assets designated as HFT or, for assets classified as AFS, in OCI until sold or impaired when such are recorded in net income.

Investments held within segregated funds continue to follow the accounting requirements in Section 4211, which are unchanged from Section 4210.

The Canadian government has announced its intention to align the current Canadian tax rules with the new financial reporting standards and released proposed tax legislation on November 7, 2007. The proposed legislation is not substantively enacted for GAAP purposes at the time of finalizing these financial statements. As a result, the Company has assumed that the current and future level of taxes paid by the Company will be consistent with existing legislation.

On adoption of the new standards, as at January 1, 2007, the Company designated its investments other than mortgages and policy loans supporting actuarial liabilities as HFT and its investments not supporting actuarial liabilities as AFS. Outstanding premiums, mortgages and policy loans are classified as loans and receivables, while other liabilities are classified as other financial liabilities, all of which are measured at amortized cost. The difference between the prior year carrying amounts and fair values on loans and receivables and other financial liabilities were not material, and therefore, no adjustments were recorded.

The impact of the adoption of these standards is as follows:

Held-for-trading

The Company designated bonds and stocks supporting actuarial liabilities with a carrying value of $317,815,000 and a fair value of $339,208,000 as HFT. The difference of $21,393,000 between the fair value and the carrying value of these investments, net of income tax of $7,998,000, at January 1, 2007 has been recorded as an adjustment to opening retained earnings. These assets were designated as HFT in order to match the measurement of the liabilities they are supporting. A significant portion of the changes in fair value of assets supporting actuarial liabilities is offset against the changes in fair values assigned to policy liabilities.

Available-for-sale

The Company designated bonds and stocks not supporting actuarial liabilities with a carrying value of $75,455,000 and a fair value of $89,561,000 as AFS. The difference of $14,106,000 between the fair value and the carrying value of these investments, net of income tax of $4,600,000, at January 1, 2007 has been recorded as opening AOCI at January 1, 2007. When these differences are realized through asset sale or impairment, gains and losses and the related tax expense previously recorded in AOCI are reclassified to net income.

Deferred gains on disposal of portfolio investments

As a result of adopting the new accounting standards, deferred gains and losses on sales of bonds and stocks previously accounted for as life insurance portfolio investments have been recorded as an adjustment of $16,178,000 to opening retained earnings, net of income tax of $4,116,000. Realized gains and losses on the sales of assets occurring on or after January 1, 2007 are recorded in investment income.

Policy liabilities

The impact of recording the investments at fair value on the selection of the discount rate and the measurement of the policy liabilities was an increase of $36,117,000 and has been recorded as an adjustment to opening retained earnings, net of income taxes of $11,779,000.

Summary of the impact of adoption on retained earnings and accumulated other comprehensive income:

	Participating policyholders	Shareholder	Total
		('000s)	
Adjustment to opening retained earnings			
Increase due to recording HFT assets at fair value	$ 12,829	$ 8,564	$ 21,393
Reversal of deferred gains on disposal of portfolio investments	8,105	8,073	16,178
Decrease due to change in actuarial liabilities	(20,529)	(15,588)	(36,117)
Decrease due to change in future income taxes	(206)	(129)	(335)
Total adjustment to opening retained earnings	$ 199	$ 920	$ 1,119
Accumulated other comprehensive income			
Increase due to recording AFS assets at fair value	$ 5,044	$ 9,062	$ 14,106
Decrease due to change in future income taxes	(1,644)	(2,956)	(4,600)
Opening balance of accumulated other comprehensive income	$ 3,400	$ 6,106	$ 9,506

Summary of the impact on the other balance sheet items as a result of adopting the new standards increase (decrease):

	As at December 31, 2006	Adjustment on adoption of new standards	As at January 1, 2007
		('000s)	
Bonds	$ 342,422	$ 16,740	$ 359,162
Stocks	50,848	18,759	69,607
Policy liabilities	350,255	36,117	386,372
Future income tax liability	1,893	4,935	6,828
Deferred gains on disposal of portfolio investments	16,178	(16,178)	–

There was no impact on reported net income for the year ended December 31, 2006.

4 SIGNIFICANT ACCOUNTING POLICIES

Premium income and benefits expense

Gross premiums for all types of insurance contracts, and contracts with limited mortality or morbidity risk, are generally recognized as revenue when due. When premiums are recognized, actuarial liabilities are computed, with the result that benefits and expenses are matched with such revenue.

Investment income

Investment income is recorded as it accrues. Dividend income on stocks is recorded on the ex dividend date. Gains and losses are determined and recorded as at the trade date, and are calculated on the basis of average cost.

The effective interest rate method is used to amortize premiums or discounts on the purchase of AFS bonds.

Available-for-sale financial assets

AFS financial assets with quoted prices in an active market are carried at fair value on the balance sheet from the trade date. Changes in fair values are recorded, net of income taxes, in AOCI until the financial asset is disposed of or has become other than temporarily impaired. When the financial asset is disposed of or has been other than temporarily impaired, the accumulated fair value adjustments recognized in AOCI are transferred to the income statement. A provision for impairment for equity instruments and debt securities classified as AFS is established when there is objective evidence that the investment is impaired and the impairment is other than temporary. Equity investments that are classified as AFS and do not have a quoted price in an active market are recorded at cost.

Held-for-trade financial assets

HFT financial assets are carried at fair value on the balance sheet from the trade date. Changes in fair values are recorded in net income. HFT financial assets are purchased or incurred with the intention of generating profits in the near term (classified as HFT) or are designated as such by the Company.

Mortgages and policy loans

Financial assets classified as loans and receivables are initially recognized at fair value and subsequently measured at amortized cost using the effective interest rate method.

Financial liabilities

Any such liabilities, other than actuarial liabilities, are initially recognized at fair value and subsequently measured at amortized cost using the effective interest rate method.

Income taxes

Future income taxes result from temporary differences in the tax basis of an asset or liability and its carrying amount in the balance sheet. The future income tax asset/liability is computed at the tax rates that are expected to apply when the income tax asset or liability is settled.

Employee future benefits

Employees of the Company are provided with pension and post employment benefits on a defined benefit basis through membership in plans offered by The Wawanesa Mutual Insurance Company. The Wawanesa Mutual Insurance Company owns 100% of the issued and outstanding shares of the Company. The obligation for funding of these plans rests with The Wawanesa Mutual Insurance Company. The Company is charged appropriate annual service costs for all benefits and remits these amounts to The Wawanesa Mutual Insurance Company.

Segregated funds

Segregated funds are investment options available to annuity contract holders in which the benefit amount is directly linked to the fair value of the investments held in the particular segregated fund. Although the underlying assets are registered in the name of the Company, and the annuity contract holder has no direct access to the specific assets, the contractual arrangements are such that the annuity contract holder bears the risk and rewards of the fund's investment performance. In addition, certain individual contracts have guarantees from the Company. The Company derives fee income from segregated funds, which is included in annuity premiums income on the statement of operations. Policyholder transfers between general funds and segregated funds are included in maturities and surrenders on the statement of operations.

5 INVESTMENTS

The carrying and fair value of the Company's investment portfolio by financial instrument classification as at December 31 is as follows:

	2007					2006	
	Classified as loans and receivables	Designated as HFT	Classified as AFS	Total carrying value	Total fair value	Total carrying value	Total fair value
			('000s)			('000s)	
Bonds	$ –	$317,845	$ 53,862	$371,707	$371,707	$ 342,422	$ 359,162
Stocks	–	37,071	30,474	67,545	67,545	50,848	69,607
Mortgages	28,394	–	–	28,394	28,412	29,053	28,846
Policy loans	13,425	–	–	13,425	13,425	13,059	13,059
	$ 41,819	$354,916	$ 84,336	$481,071	$481,089	$ 435,382	$ 470,674

The fair value for publicly traded bonds is determined using the quoted market bid prices. HFT and AFS bonds are reported at fair value as of December 31, 2007, the last market trading day of the year. The carrying value of these bonds is equal to their fair value.

Stocks are comprised of units in institutional pooled equity funds. The fair value for stocks is valued at the underlying mutual funds' transactional net asset value per unit at the end of each valuation day. Bid prices are not available for the underlying funds. HFT and AFS stocks are reported at fair value as of December 31, 2007, the last valuation day of the year. The carrying value of these stocks is equal to their fair value.

The fair value for mortgages is determined by discounting the mortgage cash flows by the Canadian yield curve plus a margin. The carrying value is the outstanding principal balances, which approximates the mortgage's amortized cost.

The outstanding balance for policy loans approximates the fair value since interest rates are set annually and approximate market rates.

Deferred realized gains on portfolio investments were credited as an adjustment to opening retained earnings on January 1, 2007, as described in note 3. Gains and losses on sale of bonds and stocks are no longer deferred and amortized into income. Included in investment income for 2006 was the amortization of net deferred realized gains for all portfolio investments and net unrealized gains of stocks.

Other net investment income is from the following sources:

	2007	2006
	('000s)	
Interest income		
Bonds	**$ –**	$ 16,432
Held-for-trading bonds	**14,961**	–
Available-for-sale bonds	**2,641**	–
Mortgages	**1,528**	1,411
Policy loans	**921**	875
Cash and other interest income	**224**	178
Dividend income		
Stocks	**–**	1,399
Held-for-trading stocks	**1,539**	–
Available-for-sale stocks	**1,422**	–
Amortization of deferred gains on disposal of portfolio investments	**–**	6,685
Other income	**71**	28
Investment expenses	**(527)**	(549)
Total other net investment income	**$ 22,780**	$ 26,459

Temporarily impaired available-for-sale assets

The AFS assets disclosed in the following table exhibit evidence of impairment, however, the impairment loss has not been recognized in net income because it is considered temporary. Financial assets designated as HFT have been excluded from the following table since changes in fair value of these assets are recorded to income. AFS assets have generally been identified as temporarily impaired if their amortized cost as at December 31, 2007 was greater than their fair value, resulting in an unrealized loss. Unrealized losses may be due to interest rate fluctuations and/or depressed fair values in sectors which have experienced unusually strong negative market reactions. In connection with the Company's investment management practices and review of its investment holdings, it is believed that the contractual terms of bond investments will be met and/or the Company has the ability to hold these investments until recovery in value.

	Fair value	Unrealized losses
	('000s)	
Available-for-sale bonds	**$ 38,177**	$ 2,135
Available-for-sale stocks	**2,448**	194
Total temporarily impaired financial assets	**$ 40,625**	$ 2,329

Terms and conditions

Details of significant terms and exposure to interest rate risk on investments are as follows:

Bonds are comprised of government 43.8% (2006 – 45.3%) and corporate 56.2% (2006 – 54.7%) with effective interest rates of 3.2% to 9.5% (2006 – 3.0% to 9.5%). Maturities range from less than one year to 39 years (2006 – one year to 37 years). Bonds with a quality rating of BBB or higher represent 100% (2006 – 100%) of the portfolio. Bonds rated A or higher constitute 98.2% (2006 – 97.6%) of the portfolio.

Stocks are comprised of units in institutional pooled equity funds. These funds include investments in common stock of major Canadian, U.S. and International companies and in Canadian corporate and government bonds. In general, stocks have no fixed maturity date and are not exposed directly to interest rate risk. Dividend yields on these funds range from 1.8% to 4.5% (2006 – 1.8% to 2.7%).

Mortgages are secured by first recourse on residential properties. Interest rates range from 4.1% to 7.5% (2006 – 3.8% to 7.5%). Virtually all are for a fixed term ranging from 6 months to 10 years (2006 – 6 months to 10 years) and 43.1% (2006 – 46.6%) of balances are insured. Principal and interest payments are received on a monthly or more frequent basis.

Policy loans have interest rates which are set annually and range from 6% to 7% (2006 – 6% to 7%).

Concentration

The Company limits its investment concentration in any one corporate investee or control group to 3% of assets.

Asset impairment

General provisions made for anticipated future losses of principal and interest on investments are included as a component of policy liabilities and are approximately $5,090,000 (2006 – $4,219,000).

Derivative financial instruments

The Company does not invest in derivative financial instruments.

6 POLICY LIABILITIES

Nature of policy liabilities

Policy liabilities represent an estimate of the amount which, together with future premiums and investment income, will be sufficient to pay outstanding claims and provide for future benefits, dividends and expenses under all in force insurance and annuity contracts. Policy liabilities consist of the following:

	2007	2006
	('000s)	
Actuarial liabilities	**$ 383,361**	$ 338,383
Provision for unpaid and unreported claims	**5,852**	6,448
Policyholder amounts on deposit	**5,606**	5,424
Total policy liabilities	**$ 394,819**	$ 350,255

Actuarial liabilities

Actuarial liabilities are comprised of the following amounts for each significant line of business:

	2007	2006
	('000s)	
Individual life participating	**$ 157,863**	$ 131,159
Individual life non-participating	**72,176**	56,702
Individual annuities participating	**49,362**	49,255
Individual annuities non-participating	**87,711**	84,380
Group life and health	**16,249**	16,887
Total actuarial liabilities	**$ 383,361**	$ 338,383

Actuarial liabilities have been determined by the Appointed Actuary using accepted actuarial practice which involves the use of assumptions for such factors as mortality and morbidity rates, future investment yields, future expense levels and rates of withdrawal. The process of determining actuarial liabilities necessarily involves the risk that actual results will deviate from assumed results. The risk varies in proportion to the length of the period covered by each assumption and the potential volatility of actual results.

Each assumption is determined based on expected experience plus a margin. The margin provides for uncertainty in establishing expected experience and to allow for possible deterioration in experience. The additional reserve resulting from using assumptions which include these margins is referred to as the provision for adverse deviations. The provision will be included in future income to the extent it is not required to cover adverse experience.

The nature and method of determining the significant assumptions made in the computation of actuarial liabilities are described below.

Mortality and morbidity rates – Estimates of future mortality and morbidity rates are based on the Company's and industry experience over extended periods.

Investment yields – Assumptions regarding future investment yields are based on current yield rates, adjusted to reflect uncertainties associated with projections of future interest rates.

Expense levels – Future expense assumptions are based on the Company's past experience and projections for the future.

Rates of withdrawal – Policyholders may lapse their policies by discontinuing premium payments or surrendering their policies for the cash surrender value. Estimates of future rates of withdrawal are based on previous Company experience augmented by industry experience.

Interest rate risk – The sensitivity analysis for interest rate risk set out below illustrates the impact of a 1% change in interest rates on the carrying value of the surplus of the Company at the reporting date. The sensitivity of actuarial liabilities to changes in interest rates is dependent on the duration of the liability. Due to the time value of money, a reduction in the interest rates would normally produce a higher insurance liability.

The approximate impact of an increase of 100 basis points in the interest yields would increase the surplus of the Company by $8,200,000. The approximate impact of a decrease of 100 basis points in the interest yields would decrease the surplus of the Company by $5,800,000

Assets supporting liabilities and capital and surplus

The following table shows the assets supporting liabilities for the product lines shown (including actuarial and other policy liabilities), and assets supporting capital and surplus as at December 31, 2007:

	2007						
	Bonds		Stocks				
	Held for trading	Available for sale	Held for trading	Available for sale	Mortgage loans	Other	Total
	('000s)						
Participating							
Individual life	**$107,702**	**$ –**	**$ 37,071**	**$ –**	**$ –**	**$ 13,090**	**$157,863**
Individual annuity	**37,440**	**–**	**–**	**–**	**11,542**	**380**	**49,362**
Non-participating							
Individual life	**69,695**	**–**	**–**	**–**	**–**	**2,481**	**72,176**
Individual annuity	**70,117**	**–**	**–**	**–**	**16,852**	**742**	**87,711**
Group life and health	**16,192**	**–**	**–**	**–**	**–**	**57**	**16,249**
Other, including capital and surplus	**16,699**	**53,862**	**–**	**30,474**	**–**	**12,308**	**113,343**
	$317,845	**$ 53,862**	**$ 37,071**	**$ 30,474**	**$ 28,394**	**$ 29,058**	**$496,704**

	2006				
	Bonds	Mortgage loans	Stocks	Other	Total
	('000s)				
Balance sheet value					
Participating					
Individual life	$ 91,152	$ –	$ 25,556	$ 14,451	$ 131,159
Individual annuity	36,851	11,988	–	416	49,255
Non-participating					
Individual life	54,764	–	–	1,938	56,702
Individual annuity	66,275	17,065	–	1,040	84,380
Group Life and Health	16,874	–	–	13	16,887
Other, including capital and surplus	76,506	–	25,292	6,482	108,280
Total balance sheet value	$ 342,422	$ 29,053	$ 50,848	$ 24,340	$ 446,663
Fair value	$ 359,162	$ 28,846	$ 69,607	$ 24,340	$ 481,955

Change in actuarial liabilities

The change in actuarial liabilities is as follows:

	2007	2006 (note 3)
	('000s)	
Balance, beginning of year as previously reported	**$ 338,383**	$ 318,156
Adjustment for change in accounting policy (note 3)	**36,117**	–
Balance, after change in accounting policy	**374,500**	318,156
Normal change		
New business	**1,510**	2,993
In force	**9,153**	18,185
Change in method and assumptions	**(1,802)**	(951)
Balance – end of year	**$ 383,361**	$ 338,383

Valuation assumptions are reviewed and updated annually. Changes in assumptions can increase or decrease actuarial liabilities. The changes in assumptions and their impact on actuarial liabilities were as follows:

	2007	2006
	('000s)	
Mortality	**$ (2,652)**	$ (364)
Lapse	**1,073**	790
Expenses	**–**	(1,763)
Other	**(223)**	386
	$ (1,802)	(951)

7 REINSURANCE CEDED

In the normal course of business, the Company limits the amount of loss on any one policy by reinsuring certain levels of risk in various areas of exposure with reinsurers.

Reinsurance ceded does not discharge the Company's liabilities as the primary insurer. Failure of reinsurers to honour their obligations could result in losses to the Company. A contingent liability exists should an assuming company be unable to meet its obligations. At December 31, 2007 the Company had outstanding balances from reinsurers totalling $1,784,200. All recoverable amounts are with reinsurers with an A.M. Best credit rating of A+ (Superior).

The retention limits or maximum exposure on insurance policies are as follows:

	2007	2006
	('000s)	
Individual Life	$ **250**	$ 200
Group Life	**150**	150
Group Health – out of country	**100**	100
Group Disability	**14/year**	14/year

The Company also has reinsurance in place for multiple deaths resulting from a catastrophic accident. Coverage is for up to $10,000,000 (2006 – $10,000,000) of claims from a single accident.

The amounts shown in the financial statements are net of the following amounts related to reinsurance ceded:

	2007	2006
	('000s)	
Premiums	$ **8,758**	$ 7,739
Claims	**6,219**	6,096
Actuarial liabilities	**46,165**	39,367

8 INCOME TAXES

The provision for income taxes reflects an effective tax rate that differs from the combined tax rate for Canadian federal and provincial corporate taxes for the following:

	2007	2006
	('000s)	
Earnings before income taxes	$ **9,522**	$ 8,252
Combined statutory tax rate	**34.87%**	35.80%
Tax payable based on statutory tax rate	**3,320**	2,954
Effect of:		
Permanent differences	**(645)**	(251)
Future income tax rate changes	**(565)**	(212)
Capital taxes	**95**	(47)
Other	**15**	(15)
	$ **2,220**	$ 2,429
Provision for income taxes		
Current	$ **34**	$ 1,346
Future	**2,186**	1,083
	$ **2,220**	$ 2,429

Future income tax assets and liabilities consist of temporary differences between the accounting and tax basis of assets and liabilities as follows:

	2007	2006
	('000s)	
Future income tax liabilities		
Invested assets	**$ 8,690**	$ 2,340
Policy liabilities	**(4,590)**	774
Deferred gains on portfolio investments	**3,660**	(1,132)
Other liabilities	**(2)**	(89)
	$ 7,758	$ 1,893

Income taxes included in OCI

Other comprehensive income included on the statement of comprehensive income is presented net of income taxes. The following income tax amounts are included in each component of other comprehensive income for the year ended December 31, 2007:

	2007	2006
	('000s)	
Unrealized gains and losses on available-for-sale assets	**$ 542**	$ –
Reclassifications to net income for available-for-sale assets	**765**	–
Total income taxes benefit included in OCI	**$ 1,307**	$ –

9 SEGREGATED FUNDS

The net asset value of the Segregated Funds, for which the Company is the issuer, totalled $140,321,000 (2006 – $129,104,000) at December 31, 2007. These Funds act as an investment vehicle for policyholders within individual savings plans. Segregated Fund policyholders bear the full investment risk of, and receive all the benefits from, the assets of the Funds. Investments held for Segregated Funds are carried at market value. Segregated Funds are presented separately in the Company's financial statements for information purposes and do not form part of the General Funds of the Company.

10 SHARE CAPITAL

Authorized – Unlimited number of common shares without par value

Issued and outstanding – 11,500 common shares, all of which have been issued for cash to The Wawanesa Mutual Insurance Company

11 TRANSFER FROM PARTICIPATING ACCOUNT TO SHAREHOLDER

From time to time, the Board of Directors sets apart a portion of participating policyholders' equity as safe and proper for distribution as dividends or bonuses to participating policyholders. Of the amount set apart, the shareholder is entitled to a portion as permitted by governing statute.

The Company converted from mutual to stock form of ownership on October 1, 1993. The plan of conversion places restrictions on transfers from the participating account to the shareholder for 5 or 15 years from the date of conversion depending on the type of policy and date of issue. Effective October 1, 1998, amounts may be allocated to the shareholder related to participating life insurance policies issued on or after October 1, 1993 and all participating annuity policies.

The shareholder is entitled to 10% of the amounts set apart for these policies on an annual basis.

12 MINIMUM CAPITAL REQUIREMENTS

OSFI requires Canadian life insurance companies to maintain minimum levels of capital with respect to their insurance operations in order to provide additional assurance with respect to future solvency. These capital levels are calculated in accordance with the Minimum Continuing Capital and Surplus Requirements (MCCSR) issued by OSFI. At the end of 2007 and 2006, the Company ratio was in excess of the regulatory minimum capital requirement.

13 RELATED PARTY TRANSACTIONS

The Company has the following transactions with its parent Company:

- The Company reimburses the cost of expenses paid on its behalf or shared with the parent totalling $11,057,000 (2006 – $10,412,000).
- The parent Company pays commissions on behalf of its brokers to investment accounts maintained by the Company of $9,039,000 (2006 – $8,399,000).
- The parent Company purchases group employee benefits from the Company at a cost of $4,594,000 (2006 – $3,674,000).

Balances between the Company and its parent are settled on a regular basis and the outstanding amount is immaterial at December 31, 2007 and 2006.

14 SEGMENTED INFORMATION

	2007				
	Individual life	Individual annuity	Group life and health	Capital and surplus	Total
	('000s)				
Premium income	**$ 33,344**	**$ 29,070**	**$ 23,456**	**$ –**	**$ 85,870**
Investment income	**4,771**	**5,461**	**542**	**6,493**	**17,267**
Income taxes	**(106)**	**914**	**340**	**1,072**	**2,220**
Net income	**(387)**	**1,187**	**1,080**	**5,422**	**7,302**
Other comprehensive loss	**–**	**–**	**–**	**(2,441)**	**(2,441)**
Total comprehensive income	**(387)**	**1,187**	**1,080**	**2,981**	**4,861**

	2006 (note 3)				
	Individual life	Individual annuity	Group life and health	Capital and surplus	Total
	('000s)				
Premium income	$ 30,995	$ 25,817	$ 23,909	$ –	$ 80,721
Investment income	13,511	5,887	1,084	5,977	26,459
Income taxes	(101)	1,163	(107)	1,474	2,429
Net income	832	1,081	(593)	4,503	5,823

15 RISK MANAGEMENT PRACTICES

The Company has developed a series of management programs that address all material risks to which the Company is exposed. Each risk management program defines the particular risk, the basis on which the risk will be measured, sets limits on risk exposure and provides for reporting on actual exposure to the Board of Directors, a designated committee of the Board or senior management.

Mortality risk

The Company is exposed to mortality risk through both individual and group policies. The insurability of applicants is determined in accordance with established and documented underwriting standards. Exposure to large claims is managed through the establishing of policy retention limits. Insurance amounts in excess of the retention limit on a single life are reinsured with other companies. The maximum retention for individual life insurance policies is $250,000 (2006 – $200,000) and the maximum retention for group life insurance policies is $150,000. The exposure to multiple claims from a single accidental cause is managed by a catastrophe reinsurance agreement. The catastrophe reinsurance covers aggregate claims in excess of $1,000,000 up to a maximum amount of $10,000,000. Claims experience (actual vs. expected) is monitored by management. This information is reported to the Board of Directors regularly.

Morbidity risk

The Company is exposed to significant morbidity risk through the issuance of group long-term disability and extended health coverages. The acceptance and rating of all health and disability applicants is determined in accordance with established and documented underwriting standards and procedures. Exposure to large claims is managed by establishing policy retention limits. Insurance amounts in excess of the retention limit on a single life are reinsured with other companies. The maximum retention for long-term disability is $1,200 of monthly benefit and for out-of-country extended health benefits is a $100,000 per incident. Morbidity claims experience is reported to the Board of Directors regularly. Senior management regularly reviews actual morbidity experience to industry studies. Claims management policies have been established and documented for all types of disability and health claims.

Lapse risk

The termination (or lapse) of individual life insurance policies may expose the Company to risk. Policyholders may lapse their policies by discontinuing premium payments or requesting surrender of their policies for the cash value. When developing a new product or pricing an existing product, the Company carefully analyzes the amount of policy termination risk. Policy termination assumptions are based on Company experience augmented by industry experience. Reinsurance is used to lessen this risk for certain plans. Company policy termination experience is monitored by senior management on a quarterly basis.

Expense risk

The Company is exposed to expense risk to the extent that future expense levels exceed those guaranteed to policyholders or assumed in the calculation of actuarial liabilities. Senior management reviews expense levels on a quarterly basis and approves expenditures of large amounts and the hiring of additional personnel.

Interest rate risk

The Company is exposed to interest rate risk in the normal course of business. The risk exists to the extent that cash flows from the assets supporting the liabilities do not match the policy obligations in timing and amount. The Company's exposure to future changes in interest rates is significantly reduced for many lines of business due to the practice of matching cash flows on the assets with those of the corresponding liabilities.

Investments are divided into four segments for purposes of investment policy related to interest rate risk. Guidelines limiting the interest rate risk to be assumed are set out by the Board of Directors in the Company's Investment Policy Statement. Techniques for measuring interest rate risk include duration analysis, cash flow analysis and yield curve sensitivity testing. The interest rate risk is monitored by management on a monthly or more frequent basis and is reported to the Investment Committee of the Board quarterly. The Company does not invest in derivative financial instruments.

Credit risk

Credit guidelines have been established by the Board of Directors and are set out in the Company's Investment Policy Statement for both the bond and mortgage portfolios. Adherence to credit guidelines is monitored on a continuous basis by management and reported to the Investment Committee on a quarterly basis.

At December 31, 2007, 100% of the bond portfolio was rated investment grade (BBB) or better with 98.2% rated 'A', 'AA', or 'AAA'. At December 31, 2007, the largest credit exposure to one corporate credit was 14.7% (2006 – 15.8%) of Policyholders' and Shareholder's Equity. The mortgage portfolio is comprised of single-family, owner-occupied dwellings in the Winnipeg, Manitoba area. At December 31, 2007, 43.1% of mortgage loans were insured with the Canada Mortgage and Housing Corporation. The largest single mortgage balance was $342,000. Mortgages with payments in arrears represented 1.9% of the portfolio.

The Company does not invest in commercial mortgages or loans.

Reinsurance risk

The Company utilizes reinsurance primarily to limit the mortality or morbidity exposure to a single life. Additional amounts of mortality risk may also be reinsured where it is in the financial interest of the Company to do so. An insignificant amount of interest rate and lapse risk is reinsured. The majority (99%) of the reinsurance business is transacted with companies registered in Canada which are subject to regulation by the Office of the Superintendent of Financial Institutions Canada. All reinsurance arrangements are approved by senior management.

Liquidity risk

The Company must maintain adequate liquidity to meet policyholder obligations as they come due. The primary obligations are annuity policy values and insurance claims and policy values.

Liquidity guidelines have been established by the Board of Directors and are set out in the Company's Investment Policy Statement. The guidelines require that the portion of the investment portfolio that is readily marketable equals or exceeds these policyholder obligations. This is monitored on a quarterly basis. Readily marketable assets include all bonds with an 'A' or better rating and all Canadian equities. At December 31, 2007, readily marketable assets represented 106.2% (2006 – 116.5%) of all policy liabilities.

16 FUTURE IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

Capital disclosures and financial instruments – disclosure and presentation

On January 1, 2008, the Company will adopt three new CICA Handbook Sections: Section 1535, Capital Disclosures, Section 3862, Financial Instruments – Disclosures, and Section 3863, Financial Instruments – Presentation. Section 1535 requires disclosure of an entity's objectives, policies and processes for managing capital; information about what the entity regards as capital; whether the entity has complied with any capital requirements; and the consequences of not complying with these capital requirements. Sections 3862 and 3863 replace Handbook Section 3861, Financial Instruments – Disclosure and Presentation. Section 3863 carries forward unchanged the presentation requirements of Section 3861 while Section 3862 requires enhanced financial instrument disclosures focusing on disclosures related to the nature and extent of risks arising from financial instruments and how the entity manages those risks. The Company will apply the new disclosures in its 2008 financial statements

17 COMPARATIVE FIGURES

Certain of the prior year's figures have been restated for comparative purposes.

1. INTRODUCTION

This Dividend Policy Statement has been adopted by the Board of Directors and a copy has been sent to the Superintendent of Financial Institutions. All dividends declared must be in accordance with this Dividend Policy Statement.

Prior to approving a dividend scale, the Board of Directors will receive a report from the Company's appointed actuary stating whether, in his opinion, the dividend scale conforms to this Dividend Policy Statement and the professional practice standards of the Canadian Institute of Actuaries on dividend determination.

2. ELIGIBILITY TO RECEIVE DIVIDENDS

Participating immediate annuity policies

Immediate annuity policies provide a periodic annuity payment for the life of the annuitant or for a specified time period. The amount of the annuity payment is comprised of a guaranteed portion and a dividend portion. No change in the dividend portion is anticipated.

Participating deferred annuity policies

These policies are accumulation annuity products which carry a guaranteed minimum rate of return. At the time a deposit is received, a current rate of interest is applied for the specified investment period. The difference between the current rate and the guaranteed rate is the dividend component.

Participating individual life insurance policies

Dividends on these policies are anticipated to be paid annually, beginning as of the end of the second policy year. The amount available to be paid as dividends is determined based on various factors including the Company's earnings, any regulatory requirements and the amount of surplus required to ensure the continuing financial stability of the Company.

The dividend scale is designed to allocate dividends in a fair and equitable manner between the classes of policyholders. The dividend scale sets out a formula for the payment to policies of distributable earnings originating from three sources; investment earnings, mortality, and expense experience. The dividend scale is designed to distribute dividends among policies in the same proportion as the policies are considered to have contributed to distributable earnings.

The dividend scale for these policies will be updated when significant changes in experience occur.

THE WAWANESA LIFE
INSURANCE COMPANY

SOURCE OF EARNINGS

The Source of Earnings are attributed to one of the following categories.

Expected profit on in-force business

This includes the release of the Provisions for Adverse Deviations (PFADs) plus the expected profits on Segregated Funds. The release of the PFADs is the profits arising on the in-force business if the expected assumptions used in calculating the actuarial liabilities are realized.

Impact of new business

This represents the overall loss during the first year on new business. The PFADs in the actuarial liabilities contribute to an over-all initial loss on issuing new business. These PFADs are anticipated to be released into income in future years to the extent they are not required to cover future adverse experience.

Experience gains and losses

The experience gains result from items such as investment returns, claims and expenses where the actual experience during the year differs from the expected experience assumed in the actuarial liabilities. It also includes the amount the fee income generated on Segregated Funds differs from expected.

Management action and changes in assumptions

This section includes specific management actions and the impact of changes in assumptions used to calculate actuarial liabilities.

Earnings on surplus

This reflects the earnings on the surplus and capital of the Company.

Other

This represents all other sources of earnings not included above.

Source of Earnings 2007	**Total Company**	**Individual Life**	**Individual Annuity**	**Group Life and Health**
		('000s)		
Expected profit on in-force business	**$ 7,258**	**$ 3,658**	**$ 1,730**	**$ 1,870**
Impact of new business	**(8,924)**	**(7,338)**	**(179)**	**(1,407)**
Experience gains and losses	**3,481**	**2,388**	**550**	**543**
Management action and change in assumptions	**1,544**	**799**	**–**	**745**
Other	**(330)**	**–**	**–**	**(330)**
Earnings on operations	**3,029**	**$ (493)**	**$ 2,101**	**$ 1,421**
Earnings on surplus	**6,493**			
Income before income taxes	**9,522**			
Income taxes	**(2,220)**			
Net income	**$ 7,302**			

Source of Earnings 2006	Total Company	Individual Life	Individual Annuity	Group Life and Health
		('000s)		
Expected profit on in-force business	$ 6,973	$ 3,524	$ 1,550	$ 1,899
Impact of new business	(7,760)	(6,215)	(133)	(1,412)
Experience gains and losses	3,200	3,138	779	(717)
Management action and change in assumptions	7	(40)	47	–
Other	(145)	324	–	(469)
Earnings on operations	2,275	$ 731	$ 2,243	$ (699)
Earnings on surplus	5,977			
Income before income taxes	8,252			
Income taxes	(2,429)			
Net income	$ 5,823			

D I R E C T O R S

B. W. Harrison 1,2,3,4
Chairman of the Board

G. J. Hanson 1,4

S. M. Van De Velde 2,3

M. E. Northey 1,2

D. G. Unruh 2,3

J. S. McCallum 3,4

R. R. Bracken 3

D. C. Crewson 1,4

K. E. McCrea 3

1. Member of the Audit Committee
2. Member of the Conduct Review and Corporate Governance Committee
3. Member of the Investment Committee
4. Member of the Human Resources Committee

Standing (L to R): G. J. Hanson, D. C. Crewson, J. S. McCallum, S. M. Van De Velde, D. G. Unruh, R. R. Bracken, M. E. Northey
Seated (L to R): B. W. Harrison, K. E. McCrea

Wawanesa

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